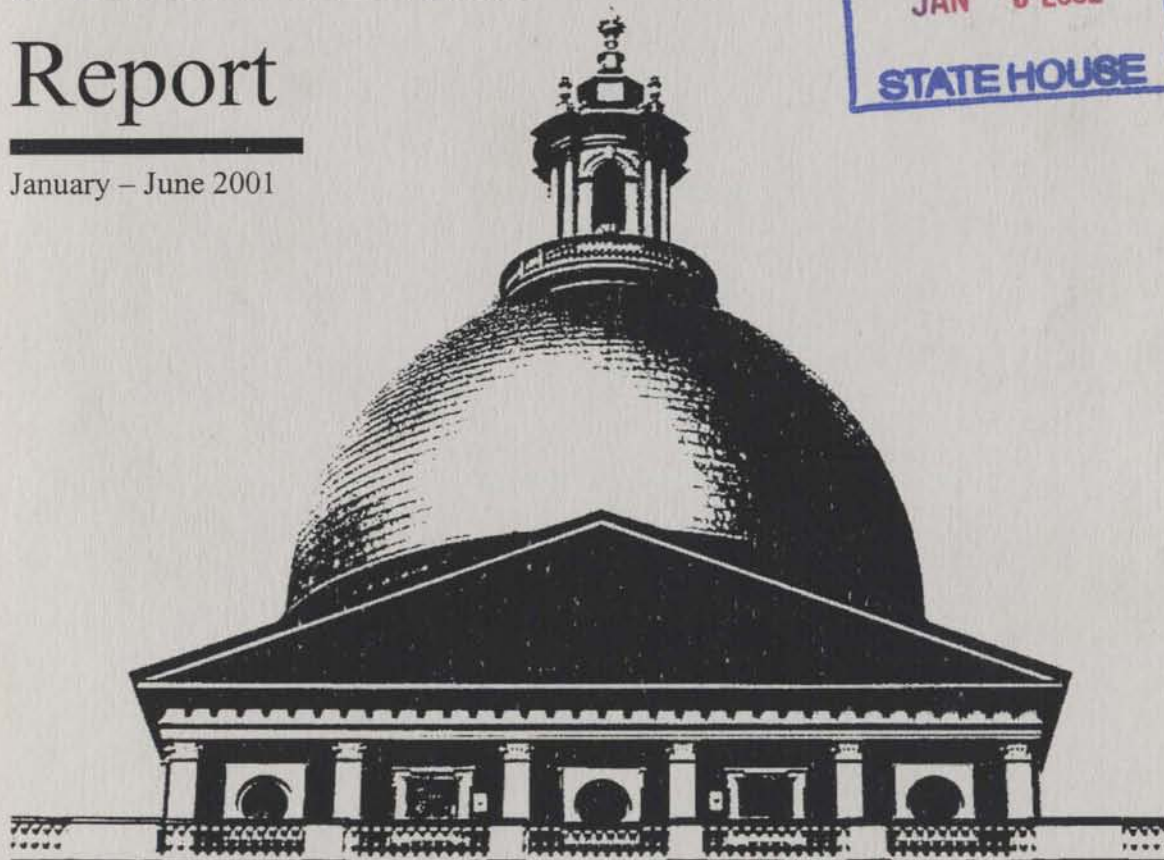
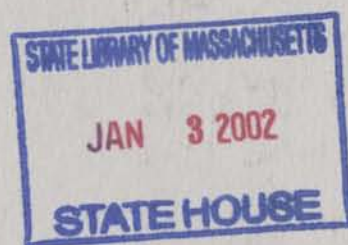


Office of the State Auditor

Semi-Annual Report

January – June 2001



Commonwealth of Massachusetts

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Joseph DeNucci, Auditor

Issue 29



The Commonwealth of Massachusetts

AUDITOR OF THE COMMONWEALTH

STATE HOUSE, BOSTON 02133

A. JOSEPH DeNUCCI
AUDITOR

TEL. (617) 727-2075

December 2001

Jane M. Swift, Governor
Thomas F. Birmingham, President of the Senate
Thomas M. Finneran, Speaker of the House of Representatives
Mark C. Montigny, Chairman of the Senate Committee on Ways and Means
John H. Rogers, Chairman of the House Committee on Ways and Means
Members of the General Court:

I am pleased to submit herewith the Semi-Annual Report of the Audit Results and Activities of the Office of the State Auditor (OSA) for the period January 1, 2001 through June 30, 2001.

This twenty-ninth report continues to present audit results organized by recurring findings within sectors of government to highlight systemic problems as well as broad areas in need of strengthening. The report also acknowledges within each section corrective actions taken by agencies in response to previous OSA audit findings or recommendations. Also included are activities of the OSA's Information Technology Audit Division and the OSA's Division of Local Mandates. Finally, proposed and ongoing initiatives are included to inform officials and the public of significant audit activity.

Copies of individual audit reports are available by calling Jay Mofenson at (617) 727-2075. Recent audits, DLM studies, and semi-annual reports can also be downloaded from the OSA's website (<http://www.magnet.state.ma.us/sao/>).

I look forward to continuing to work with you for the improvement of the quality, cost-effectiveness, and accountability of state government and the services that the Commonwealth provides its citizens.

Sincerely,

A. Joseph DeNucci
Auditor of the Commonwealth

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Office of the Auditor of the Commonwealth

AUDITOR OF THE COMMONWEALTH

STATE HOUSE, BOSTON 02125



July 1, 2001

August 2001

James M. Bell, Governor
Thomas F. Eagar, President of the Senate
Thomas M. Ichniowski, Speaker of the House of Representatives
Mark C. Montigny, Chairman of the Senate Committee on Ways and Means
John F. Rogers, Chairman of the House Committee on Ways and Means
Members of the General Court

I am pleased to submit herewith the Twenty-Ninth Report of the Audit Results and
Activities of the Office of the Auditor (OEA) for the period January 1, 2001 through
June 30, 2001.

The twenty-ninth report continues to present audit results organized by recurring
themes within sections of government to highlight systemic problems as well as present
areas in need of strengthening. The report also contains a section on
constructive actions taken by agencies in response to previous OEA audit findings or
recommendations. Also included are activities of the OEA's Information Technology
Audit Division and the OEA's Division of Local Initiatives. Finally, proposed and
ongoing initiatives are included to inform officials and the public of significant audit
activity.

Copies of individual audit reports are available by e-mailing info@oer.state.ma.us or by calling 1-800-352-1237.
2001 Report audit, OEA's website and summary report can also be downloaded
from the OEA's website (<http://www.oer.state.ma.us>).

I look forward to continuing to work with you for the improvement of the quality, cost,
effectiveness, and accountability of state government and the services that the
Commonwealth provides to citizens.

Thomas M. Ichniowski
Auditor of the Commonwealth

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Office of the State Auditor: Authority and Responsibilities

The Office of the State Auditor (OSA) operates under the direction of the State Auditor, A. Joseph DeNucci, an independently elected constitutional officer. The OSA provides the Governor, the Legislature, auditees, oversight agencies, and the general public with an independent evaluation of the various agencies, activities, and programs operated by the Commonwealth. As mandated by Chapter 11, Section 12, of the Massachusetts General Laws (MGLs), the State Auditor conducts audit work at least once every two years at all departments, offices, commissions, health and higher education institutions, and agencies of the Commonwealth, including its court system and authorities. Not including special audit projects, the number of primary entities requiring audit coverage totals approximately 500. The Auditor also performs audits of vendors and contractors that do business with the Commonwealth and its instrumentalities. Furthermore, under Chapter 7, Sections 52 through 55, MGLs, the Auditor has mandated responsibilities relative to privatization initiatives. In addition, the Auditor is responsible, under Chapter 11, Section 6B, MGLs, for the Division of Local Mandates, which is charged primarily with determining the financial impact of legislation and regulations on cities and towns.

The OSA conducts financial, performance, and Information Technology audits in accordance with "Government Auditing Standards" issued by the Comptroller General of the United States. These standards are known in the profession both as Generally Accepted Government Auditing Standards and as the Yellow Book standards.

OSA audit activities include the following objectives:

- Attesting to the fair presentation, accuracy, and reliability of an auditee's financial statements;
- Determining whether the Commonwealth's resources are properly safeguarded;
- Determining whether such resources are properly and prudently used;
- Determining an auditee's compliance with legal and regulatory requirements;
- Obtaining an understanding of an entity's internal control structure;
- Evaluating management's economy and efficiency in its use of resources;
- Determining and evaluating a program's results, benefits, or accomplishments; and
- Ensuring that all audit results are disclosed to the public and the auditees.

All OSA audit results and recommendations are intended to assist agency and program administrators by indicating areas where accounting and administrative controls, financial operations, program results, and efficiency and effectiveness can be improved. The OSA also offers technical assistance where appropriate. In short, the OSA is not simply a critic but is an agent, an advocate, and a catalyst for improved management and delivery of government services.

Audit Results, Recommendations, Initiatives, and Corrective Actions: Overview

During the report period January 1, 2001 through June 30, 2001 the Office of the State Auditor issued reports covering 198 agencies, authorities, institutions of public higher education, human service entities, judiciary/law enforcement entities, and various other state activities. For a complete listing of audit reports, see the Appendix on page 94. In these reports the OSA disclosed millions of dollars in financial and operational deficiencies and provided recommendations intended to safeguard the Commonwealth's assets and to improve the effectiveness and efficiency of governmental operations.

Each type of entity audited by the OSA is governed by particular laws and regulations; is required to maintain financial records properly; and is expected to operate economically and effectively. OSA audits are not intended to sensationalize, but rather to present an accurate appraisal of financial management, legal compliance, and, where appropriate, program effectiveness and efficiency.

Audit results and recommendations are important to auditees, and in a majority of instances auditees have indicated a willingness to take appropriate corrective actions. Audit results, viewed in the aggregate, give focus to problem areas for legislators and administration officials and, along with critical individual audit results, are the basis of OSA legislative and administrative initiatives and recommendations.

The following information demonstrates that OSA audits have promoted the safeguarding and enhancement of the Commonwealth's assets and also have assisted auditees in creating solutions that improve their financial and managerial operations.

Education Audits

During the report period, the OSA released audits covering seventeen education entities. One of these reports reviewed Information Technology (IT) activities and is detailed in the IT Audit Section, which begins on page 61.

Overview

The following information summarizes the OSA audits that have been conducted since the beginning of the current fiscal year. The OSA has conducted audits in various areas, including financial, operational, and programmatic. The OSA has also conducted audits of public entities, including state universities, state colleges, and state departments. The OSA has also conducted audits of private entities, including non-profit organizations and for-profit companies. The OSA has also conducted audits of federal agencies, including the Department of Education and the Department of Health and Human Services. The OSA has also conducted audits of state agencies, including the Department of Education and the Department of Health and Human Services. The OSA has also conducted audits of local government entities, including cities, counties, and municipalities. The OSA has also conducted audits of private entities, including non-profit organizations and for-profit companies. The OSA has also conducted audits of federal agencies, including the Department of Education and the Department of Health and Human Services. The OSA has also conducted audits of state agencies, including the Department of Education and the Department of Health and Human Services. The OSA has also conducted audits of local government entities, including cities, counties, and municipalities. The OSA has also conducted audits of private entities, including non-profit organizations and for-profit companies.

Each type of entity audited by the OSA is governed by particular laws and regulations; is required to maintain financial records properly; and is expected to operate economically and effectively. OSA audits are not intended to police or punish, but rather to prevent an accurate appraisal of financial management, legal compliance, and, where appropriate, program effectiveness and efficiency.

AUDIT RESULTS

Deficiencies in Contract Procurement and Oversight

The execution of formal contracts, in conjunction with adequate contract monitoring, helps to contain contract costs and to ensure contract performance. The following entities needed to improve contract administration controls.

- The Department of Education's (DOE) Community Partnerships for Children program (CPC) needed to improve its contracting procedures. Specifically, seven of the thirteen CPCs reviewed had not entered into formal written contracts with all of their service providers. During the audit period, these seven CPCs expended \$910,351 for subcontracted services for which there was no contract. In addition, at five of the thirteen CPCs reviewed, subcontracts totaling \$387,165 were not properly executed in that they lacked signatures or required information, such as unit rates for service or a specified maximum contract obligation.
- The Department of Education's (DOE) Community Partnerships for Children program (CPC) needed to strengthen the monitoring of subcontractor billings. For example, one CPC program gave \$240,000 to four daycare providers, which they used to improve and expand their daycare facilities. However, since these capital expenditures primarily benefited non-CPC children, they represented an unallowable program expense to the state. In addition, six subcontractors retained parent fees totaling \$171,066 that were required offsets against the state's program liability; fourteen subcontractors failed to return unexpended CPC funds totaling \$46,661 to lead agencies; five subcontractors received duplicate payments totaling \$8,092; and four subcontractors overcharged \$9,097 for classroom attendance.

Deficiencies in Contract Procurement and Oversight (continued)

- The Department of Education (DOE) allowed questionable consultant hiring practices in its Information Technology (IT) division. Two consultants working as directors in the IT division hired three family members. One of the hirees, the sister of a director, was paid \$87,447 during fiscal years 1999 and 2000 to work from home. In addition, a consultant working at DOE as the IT Procurement Coordinator was also the President of one of the consulting companies doing business with DOE. This individual participated in the procurement and payment of \$2,683,932 in expenses that were passed through his own company and, for which, his company received an estimated \$243,994 in markups. These practices were indicative of serious potential conflict-of-interest issues.
- The Department of Education (DOE) did not execute formal written contracts for its IT consultant services. Without formal documentation relative to scope of services, rate of compensation, or term of employment, DOE lacked an effective mechanism for monitoring contract performance. Furthermore, DOE violated state law by allowing consultants to supervise state employees, by employing consultants for extended periods of time, and by providing some consultants with state benefits such as health insurance and paid holiday leave.

Inadequate Accounting and Administrative Controls

Adequate accounting and administrative controls help to ensure that state funds are spent properly and efficiently. They also assist in ensuring compliance with the specific laws, rules, regulations, and guidelines that govern individual state and contract programs. The following internal control issues were noted.

- The Department of Education (DOE) had not established adequate internal controls to effectively implement, evaluate, monitor, and report the activities of the Community Partnerships for Children (CPC) program, which received over \$93 million in state funding for fiscal year 2000. Specifically, DOE did not perform any field audits to validate information provided by CPCs and was unaware that significant discrepancies existed between information reported by CPCs and their actual activities as detailed in their records. Moreover, DOE did not require CPCs to submit sufficiently detailed expenditure information and consequently could not determine the extent to which each CPC expended funds on direct program services.
- The Department of Education (DOE) needed to improve program guidelines for its Community Partnerships for Children (CPC) program. Specifically, DOE guidelines did not address the need to reassess program eligibility on a regular basis; did not provide specific instructions for CPCs to follow regarding the development, maintenance, and utilization of waiting lists; did not instruct CPCs on reimbursement policies for absent days; did not adequately define a process for CPCs to follow when calculating and documenting family income; and did not require CPCs to develop and implement cost allocation plans for expenses that benefit CPC and non-CPC children. These deficiencies resulted in numerous inconsistencies from one region to another in the delivery of CPC program services.

Inadequate Accounting and Administrative Controls (continued)

- The Department of Education (DOE) allowed Community Partnerships for Children (CPC) program funds received for direct program services to be reallocated to other budget expense categories. The budget changes requested by the thirteen CPC programs visited by OSA auditors were approved by DOE without exception and resulted in unnecessary, unallowable, and untimely purchases of supplies, equipment, and services totaling approximately \$1.1 million. Moreover, the spending frequently occurred near the close of the fiscal year, which resulted in purchases being received in the following fiscal year, contrary to state regulations.
- The Department of Education's Community Partnerships for Children program (CPC) needed to improve the functioning of Community Partnership Councils in order to consistently operate as a collaborative service, as required by law. The audit noted that some Councils did not have adequate bylaws, did not properly maintain meeting minutes, and did not have representation from required groups. Furthermore, average attendance at CPC Council meetings was as low as 23%, and several members, including those whose organizations received local CPC funding, rarely or never attended meetings. As a result of this lack of collaboration, there was inadequate assurance that CPC program services were being coordinated and delivered in an optimal manner.
- The Department of Education (DOE) did not have adequate controls over payroll expenditures for its Information Technology (IT) division. Specifically, DOE did not have formal written procedures for documenting and maintaining attendance of IT personnel. Furthermore, there was no documentation to support \$1,687,509 in payroll expenses charged by a consulting company; consultants signed payroll authorizations for themselves, other consultants, and state employees; and discrepancies existed between the Chief Technology Officer's daily attendance calendar and the weekly time log from which payroll expenditures were calculated. The OSA recommended that DOE implement standard recordkeeping and payroll authorization procedures for the whole agency.

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- The University of Massachusetts at Amherst did not adequately segregate duties relative to its Procurement Credit Card (Procard) Program. Under the Procard Program, which has more than one thousand authorized cardholders, participating employees are allowed to charge to the University small purchases of approved supplies or services. Although there were written procedures and documented controls in place for this program, they did not require an adequate separation of duties in that they allowed an employee to make improper charges totaling \$3,202 and to divert \$376 in petty cash funds for his own use. Pursuant to the requirements of Chapter 647 of the Acts of 1989, the Internal Control Statute, the OSA made recommendations for strengthening the control environment. In addition to suggesting that duties be segregated so that the work of one employee can act as a check on that of another, the audit recommended that the University limit Procard usage to individuals directly involved in procurement functions. The audit also noted that the University delayed the reporting of the suspected improper credit card charges and did not report the petty cash theft. The Internal Control Statute requires that all variances, losses, shortages, and thefts be immediately reported, so that the OSA can, as quickly as possible, determine the full extent of the problem and recommend corrective action to prevent similar occurrences in the future. See page 76.
 - The University of Massachusetts at Amherst needed to improve compliance by individual cardholders with guidelines issued for its Procurement Credit Card (Procard) Program. In a sample test of 613 expenditure transactions totaling \$82,754 from 53 authorized cardholders, 58 transactions totaling \$29,059 were not in compliance with certain conditions of the Procard User Guide. Noted noncompliance issues included same-day purchases in excess of the \$500 daily limit, a lack of bank statement reconciliations, use of unauthorized vendors, unmaintained receipts, and unapproved business, entertainment, and personal purchases. In addition, the audit noted that replacements for lost, stolen, or missing cards were issued without a new authorization agreement, and background checks were not conducted prior to issuance of credit cards.
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Questionable or Unallowable Billings and Expenditures

The OSA conducted an audit of Information Technology (IT) expenses incurred by the Department of Education (DOE) during fiscal years 1999 and 2000. Results of this review, which disclosed millions of dollars in unnecessary, undocumented, and questionable expenditures, as well as noncompliance with state laws relative to the use of consultants, are detailed below.

- DOE used consulting companies as fiscal conduits to hire consultants to work in its IT division. Although many of these consultants were recruited, interviewed, and hired by DOE, they were placed on the payrolls of various IT consulting companies. The consulting firms then sent the individuals back to DOE, charging an hourly fee that represented the individual's salary plus a markup for each consultant. Using this hiring method, DOE, over a two-year period, paid \$399,950 for one consultant and \$373,016 for another. The markup (or profit margin) for 23 consultants whom DOE officials agreed they had recruited and hired totaled \$361,635 during the two-year period. Furthermore, had DOE hired all of its IT consultants directly, it could have saved at least \$3,652,433 in consultant salary costs over that period.

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- DOE used two of its IT consulting firms to pay non-personnel and personnel expenses. Specifically, bills for various DOE expenses were sent to and paid for by a consulting company. The firm then sent a bill to DOE for the charge plus a markup of as much as 10% for payment processing. Use of these fiscal conduits cost DOE as much as \$289,587 in unnecessary non-personnel expenditures. Furthermore, DOE paid a consulting company \$288,030 to purchase office furniture and rent office space rather than competitively procuring them as required by state regulations. Finally, the audit identified thousands of dollars paid by DOE for expenses that did not seem to directly benefit DOE's operations. These questionable expenses included more than \$194,000 to provide training for consultants who purportedly had been hired for their expertise; \$309,575 for cellular phones and pagers for consultants and for telephone lines in consultants' homes; \$48,381 for food for consultant meetings; \$677 for flowers; \$1,237 for Christmas parties for consultants; \$202 to repair the windshield of a consultant's automobile; and \$227 in annual fees and finance charges on personal credit cards for two consultants. DOE also had inadequate documentation to support \$3,245,633 in non-salary IT expenses, including \$227,698 for which DOE had no documentation and \$615,505 in payments made by a consultant to himself and the company that employed him. Finally, DOE violated state finance laws by prepaying \$143,530 for IT consultant services before these services were rendered and misclassified thousands of dollars in IT expenditures in its report to the State Comptroller.
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INITIATIVES

The following is an update of ongoing initiatives in the area of education.

Review of Charter Schools

- The OSA has completed a review of the Department of Education's monitoring and oversight activities relating to charter school operations. This audit, which will be detailed in the next Semi-Annual Report, is available from the Office of the State Auditor at (617) 727-2075.

Student Financial Aid Programs

- The OSA is continuing audits of federal student financial assistance programs at the Commonwealth's institutions of public higher education.

Health and Human Services Audits

During the report period, the OSA issued audits pertaining to forty health and human service entities and contractors. One of the reports issued reviewed the Department of Public Health's Childhood Lead Poisoning Prevention Program and made recommendations for addressing delays by private laboratories in reporting instances of lead poisoning in children. Another of these reports reviewed Information Technology (IT) activities and is detailed in the IT Audit Section, which begins on page 61.

• The Fernald Developmental Center's fiscal office did not properly monitor the financial activities of its staff account. Specifically, fiscal management did not monitor report preparation of the staff's cash balances and did not ensure timely deposit of cash receipts. Furthermore, certain payments for food and paper products were made in cash, out of cash register receipts, rather than by check. In addition, financial duties were not adequately segregated, and the staff committee did not have required number or mix of committee members. As a result, there was inadequate assurance that staff funds were administered for the benefit of the residents and adequately safeguarded against loss, theft, or misuse.

Audit Results

Deficiencies in Contract Procurement and Oversight

The execution of formal contracts, in conjunction with adequate contract monitoring, helps to contain contract costs and to ensure contract performance. The following entities needed to improve contract administration controls.

- Project COPE, Inc., a not-for-profit company that contracts with the Commonwealth to provide substance abuse and behavioral health services, had not established adequate written policies and procedures relative to the procurement of goods and services. Specifically, Project COPE did not document its need for consultant and other services it procured, did not award most of its contracts using a competitive bid process, and did not clearly delineate the scope of services contractors were to perform. As a result, there was inadequate assurance that the entity contracted for only necessary services, received the highest quality services at the lowest cost, or had an effective mechanism for monitoring contract performance.

Inadequate Accounting and Administrative Controls

Adequate accounting and administrative controls assist entities in maximizing revenue potential and minimizing vulnerabilities to waste and lost income. They also assist in ensuring compliance with the specific laws, rules, regulations, and guidelines that govern individual state and contract programs. The following internal control issues were noted.

- The Department of Public Health's (DPH) Childhood Lead Poisoning Prevention Program lacked the control procedures needed to ensure compliance with mandatory reporting regulations and, in fact, did not receive laboratory tests in a timely manner. For example, private laboratories with which DPH contracted for blood tests reported blood analyses an average of three to seven days beyond the mandated one-week guideline, and four of the 32 private laboratories averaged at least 25 days to report their blood test results. Of particular concern, these four laboratories neglected to report 13 known cases of lead poisoned children within the program's mandatory three business days. Private laboratory reporting delays deprived lead-poisoned children from timely treatment and posed a serious threat to their prospects for recovery.
- The Fernald Developmental Center's fiscal office did not properly monitor the financial activities of its café account. Specifically, fiscal management did not monitor report preparation or the café's cash balances and did not ensure the timely deposit of cash receipts. Furthermore, certain payments for food and paper products were made in cash, out of cash register receipts, rather than by check. In addition, financial duties were not adequately segregated, and the café committee did not have the required number or mix of committee members. As a result, there was inadequate assurance that café funds were administered for the benefit of the residents and adequately safeguarded against loss, theft, or misuse.

Audit Results

Inadequate Accounting and Administrative Controls (continued)

- Tewksbury Hospital did not have a written internal control plan that addressed its financial and programmatic operations as required under Chapter 647 of the Acts of 1989, The Internal Control Statute. As a result, the Hospital could not be assured that it was properly safeguarding its assets and maximizing operational efficiency. Hospital officials took immediate corrective action and initiated development of an internal control manual based upon guidelines prepared by the Office of the State Comptroller.
- Tewksbury Hospital's maintenance department employees did not prepare and sign their own time records. Moreover, the summary time sheets prepared for them did not indicate actual times employees started and ended either a regular shift or overtime work. In addition, overtime pay, which totaled \$193,003 in fiscal year 2000, was not pre-approved by an appropriate supervisor and was not identifiable to a particular project or task. As a result of these weaknesses, there was inadequate assurance that all payments made to maintenance department employees was for time actually worked.

Inadequate Controls over Patient Accounts

Strict monitoring of patient funds, along with proper accounting controls, is necessary in order to ensure accurate account balances, proper fund expenditures, and appropriate interest income. The need for improved management of these funds was noted in the following instances.

- The Fernald Developmental Center was cited in a prior audit for deficiencies in the management of certain client funds. While the Center had begun to take steps to return funds belonging to discharged or deceased clients, it still retained \$120,464 owned by 27 deceased clients and ten discharged patients. Moreover, funds belonging to 17 deceased clients identified in the prior audit had still not been returned to the rightful owners. In addition, the Center continued to have inadequate internal controls over the disbursement of client funds when procuring items for resident clients. Specifically, the audit noted insufficient documentation of disbursements, the untimely return of unspent client funds, and checks issued to shoppers rather than vendors. Continued inadequate internal controls exposed client funds to potential theft, loss, or misuse.
- The Monson Developmental Center had not instituted uniform practices and requirements for the disposition of deceased clients' funds. As a result, the Center was holding \$24,510 in funds belonging to 35 deceased clients for excessively long periods of up to nine years. The Center also retained burial trust accounts that had been established for six clients, one of whom had been deceased for seven years. The Center, in response to these findings, began contacting guardians and family members to assist in the disposition of decedents' accounts.

Inadequate Controls over Property and Equipment

All state and private entities that receive funding for the purchase of equipment are required to keep complete inventories of fixed assets to ensure that the property is safeguarded and used for its intended purposes. The following reports identified areas where inventory controls needed improvement.

- The Fernald Developmental Center, while in partial compliance with the Commonwealth's fixed-asset requirements, did not have a complete fixed asset listing. Specifically, 776 items did not have a listed value, and 179 items had not been assigned a property identification number. In addition, fixed-asset testing found that 40 out of 105 items could not be located, and 27 items that were physically located could not be found on the listing. Finally, clerical errors caused the inventory to be overvalued by \$811,107, and equipment totaling over \$250,000 that was located in closed buildings had not been subject to a physical inspection. As a result of these deficiencies, the Center could not be assured that its fixed assets were properly safeguarded or accurately reported on financial statements.
- The Soldiers' Home of Massachusetts (Chelsea) did not comply with the Commonwealth's fixed-asset and management reporting responsibilities. The Home did not conduct required physical inventories, did not maintain a complete fixed-asset listing, and did not accurately record and report all equipment purchases. As a result, the Home could not be assured that its assets were adequately safeguarded against loss, theft, or misuse.
- Project COPE, Inc., did not maintain adequate information relative to its inventory of fixed assets, which totaled \$90,284. In addition, Project COPE did not identify the source of funds that were used to purchase each asset. As a result, there was inadequate assurance that the depreciation expenses totaling \$17,595 that Project COPE charged to state programs during fiscal year 1999 were accurate.
- Tewksbury Hospital was cited in a prior audit for fixed-asset deficiencies. The current review noted that a complete physical inventory had still not been taken; several items could not be found or were located in an area other than the location indicated on the inventory listing; and value listings were not always accurate. As a result, the Hospital could not be assured that its fixed assets were adequately safeguarded or accurately recorded on financial reports.

Questionable or Unallowable Billings and Expenditures

The following examples of questionable or unallowable charges and reimbursements, which reduce funds available for service provision, were noted.

- Project COPE, Inc., could not document that all of the \$267,536 it received from the Department of Public Health (DPH) for outpatient services utilized the Commonwealth as the payer of last resort, as required. As a result, there was inadequate assurance that all of the billings submitted to and reimbursed by DPH for outpatient services were allowable. The audit did note that Project COPE adhered to and adequately documented insurance coverage and fees relative to services it provided in its Batterers Intervention Program and Multiple Offender Program.
- Project COPE, Inc., provided a one-time salary bonus totaling \$19,732 to certain members of its staff, of which \$12,745 was charged to its state contracts. However, contrary to state regulations, the entity did not provide notice of this bonus to its state purchasing agencies prior to incurring these costs and did not make the bonuses available to all employees under an established written policy. As a result, these expenses were unallowable and nonreimbursable under its state contracts.
- Project COPE, Inc., during the audit period, billed the Department of Public Health (DPH) at least \$5,823 for expenses that were either not adequately documented or not directly related to the social service purposes of its state-funded programs. These billings were for items such as flowers, food, gifts, alcoholic beverages, and travel. Under state regulations, such expenses are unallowable under state contracts and should be recovered by DPH.

Prior Audit Results: Corrective Actions

A review of prior audit results is an important component of each OSA audit. This follow-up review helps to monitor and recognize agency compliance with OSA recommendations. The following entities have taken corrective actions as recommended by the OSA.

The Monson Developmental Center

- The Center has established an Information Technology (IT) Executive Steering Committee to strengthen accountability and improve management and security relative to IT-related issues. Under its direction, control procedures for IT program modifications and system changes have been implemented, and an inventory of software has been completed.

Tewksbury Hospital

- The Hospital has improved controls over its canteen fund operations, cash management, and patient fund accounts. Hospital officials have also resolved an outstanding issue relative to occupancy of hospital property.

Initiatives

The following is an update of planned and ongoing initiatives in the area of health and human services.

Department of Mental Retardation (DMR): Leasing and Purchasing Activities

- The OSA is reviewing DMR's policies and practices for leasing and purchasing community residences for its clients. The audit will include an examination of costs associated with DMR's lease/purchase activities as well as compliance and procedural issues.

Review of State-Funded Day Care Services

- The OSA is conducting a statewide audit to determine the extent to which state-funded day care services are available to eligible families throughout the Commonwealth. This review will include audit work at the Office for Child Care Services (OCCS), the Department of Education (DOE), and selected day care providers. At each state agency, the audit will review regulations, guidelines, and policies governing day care programs; identify the day care services currently offered; determine the total state funding provided for each target population; and identify each agency's service providers. The audit will also include efforts made by OCCS and DOE to coordinate the delivery of day care services and to identify those geographical areas in need of additional service.

Prior Audit Results: Corrective Actions

Independent and Housing Authority Audits

During the report period, the OSA issued reports relative to 67 independent entities, 38 of which were federally mandated audits of state-administered federal and state programs. One of these audits, which reported on Massachusetts Turnpike Authority oversight activities associated with the proposed North/South Rail Link in Boston, is detailed in a section on the Central Artery/Third Harbor Tunnel, which begins on page 54. One audit reviewed Information Technology (IT) activities and is detailed in the IT Audit Section, which begins on page 61.

Audit Results

Inadequate Accounting and Administrative Controls

Adequate accounting and administrative controls assist entities in maximizing revenue potential and avoiding unnecessary deficits, thereby helping to increase funds available for operations and services.

- The Massachusetts Community Development Finance Corporation (CDFC) did not have written policies and procedures regarding internal accounting and administrative controls. As a result, staff lacked proper guidance in several areas, including the maintenance of payroll and contract controls. CDFC did not have sufficient documentation, such as time and attendance records, to support its payroll costs and, consequently, could not be assured that all payroll expenditures were for time actually worked. In addition, the agency did not have signed contracts for three consultants and, therefore, lacked a mechanism for monitoring consultant costs and performance.
- The Massachusetts Technology Park Corporation (MTPC) had not established policies and procedures relative to consultant procurement and administration. One result of this deficiency was that MTPC made numerous questionable and improper consultant payments. These included payments made under purchase orders rather than contracts, payments made under expired or unsigned contracts, and payments made without either a purchase order or a contract. In addition, because contract controls were inadequate, MTPC did not have a reliable mechanism for monitoring or enforcing consultant performance.

Inadequate Accounting and Administrative Controls

(continued)

- The Massachusetts Technology Park Corporation (MTPC) did not have adequate internal controls over the use of its credit cards to pay for travel-related expenditures. For example, MTPC did not require individuals who used corporate credit cards to submit original receipts to substantiate the validity of their expenditures. Further, employees who paid for business-related travel costs by corporate credit cards may have also been reimbursed for these same charges as out-of-pocket expenses. Apparently, the business manager compared employee expense reports to credit card statements and deducted duplicate claimed charges from the employee's expense report. This was deemed an inadequate system for preventing duplicate payments, especially since staff members using credit cards and submitting expense reports were not required to sign truth and accuracy forms subject to penalties. Under the practices in place during the audit period, 68% of travel expenditures reviewed were found to be questionable.
- The Massachusetts Technology Park Corporation (MTPC) had not established an investment policy to ensure that all cash was adequately invested to maximize its total return. The audit noted, for example, that \$105,386 was deposited in a non-interest-bearing checking account with Fleet Bank. Furthermore, during May 2000, when field audit calculations were made, investing at least a portion of the \$84,057,620 MTPC had deposited with the Massachusetts Municipal Depository Trust, a money market investment vehicle of the Commonwealth, in Certificates of Deposit, would have yielded thousands of dollars in additional interest income.

Prior Audit Results: Corrective Actions

- Massachusetts Bay Transportation Authority (MBTA)

■ The Massachusetts Technology Park Corporation (MTPC), during the period July 1, 1998 to May 31, 2000, paid over \$364,814 to employees for annual performance, holiday, and other types of bonuses. The entity also paid a total of \$26,464 for the buy-back of earned time to its Executive Vice-President/General Counsel. These expenditures were questionable in that they were not made in accordance with up-to-date approved employee policies and procedures. In fact, neither MTPC's Employee Handbook, dated June 26, 1996, nor a one-page employee benefit summary provided to auditors to reflect current benefits mentioned payments for bonuses or purchases of earned time. MTPC officials responded that they were in the process of updating their Employee Handbook. This process should include review and approval by MTPC's Board of Directors, who are responsible for ensuring that employee benefit payments, such as bonuses and buy-backs of earned time, are consistent with the entity's mission as defined in its enabling statute.
- Massachusetts Bay Transportation Authority (MBTA)

■ The Massachusetts Water Resources Authority (MWRA) could have avoided additional project costs of \$13.8 million associated with the removal of diffuser plugs in the outfall tunnel at Deer Island. While recognizing that construction of the outfall tunnel was an extremely complex and difficult project involving millions of dollars in unavoidable change orders, the audit noted areas in which improved contract monitoring could have prevented costly delays. For example, the MWRA could have had the original diffuser plug removal plan validated by independent tunnel safety experts and required that contractors certify their compliance with federal Occupational Safety and Health Administration requirements.
- Massachusetts Port Authority (Massport)

■ The OSA is continuing a review of Massport's management activities. An audit in progress is currently reviewing Massport's property management system with emphasis on utilization and revenue generation, as well as the administration of lease and rental agreements. The audit will also review policies and procedures for tracking and collecting rental income and will determine whether lease and rental rates are adequate and appropriate.

Prior Audit Results: Corrective Actions

A review of prior audit results is an important component of each OSA audit. This follow-up review helps to monitor and recognize agency compliance with OSA recommendations. The following housing authorities have taken corrective actions as recommended by the OSA.

Leicester Housing Authority

- The Authority, during the audit period, utilized a competitive bidding process for all projects that exceeded \$10,000.

Worcester Housing Authority

- The Authority has corrected variances that existed between balances recorded in its general ledgers and those reported on state and federal financial statements. Although the Authority still needed to improve certain aspects of its reconciliation process, accurate financial statements for the fiscal year ended March 31, 2000 were filed with the Department of Housing and Community Development in September 2000.

Initiatives

The following is an update of planned and ongoing OSA initiatives in the area of authority audits.

Massachusetts Bay Transportation Authority (MBTA)

- The OSA is continuing to review and analyze the MBTA's capital improvement and expansion plan, as well as overall management activities. This audit will result in a series of reports, five of which have been issued. Currently, the OSA is examining contract procedures and costs associated with Red Line improvements, Authority-wide commuter parking, and master leases at South Station, North Station, Alewife Station, and the Orange Line. The five issued reports pertain to the construction of a new police headquarters at Newmarket Square, the Blue Line Rehabilitation and Improvement Project, Commuter Rail Activities, Elevator and Escalator Maintenance, and construction of the South Station Transportation Center.

Massachusetts Bay Transportation Authority (MBTA)

- The OSA is conducting an audit of the MBTA's privatization contract for real estate management. This review focuses on selected transactions conducted by the contractor, including but not limited to development projects, surplus property sales, leases, and easements. The audit is reviewing these transactions to determine whether they were conducted in conformity with the contract and with competitive contracting requirements. The audit will also examine the appropriateness of all fees, commissions, and bonuses earned; the adequacy of documentation to support transactions; and oversight of the selected transactions.

Massachusetts Port Authority (Massport)

- The OSA is continuing a review of Massport's management activities. An audit in progress is currently reviewing Massport's property management system with emphasis on utilization and revenue generation, as well as the administration of lease and rental agreements. The audit will also review policies and procedures for tracking and collecting rental income and will determine whether lease and rental rates are adequate and appropriate.

Prior Audit Results: Corrective Actions

Judiciary/Law Enforcement Audits

During the report period, the OSA issued seven judiciary/law enforcement audits, including investigations of missing funds at Barnstable County Superior Court and the Andover Police Relief Association. One of these reports reviewed Information Technology (IT) activities and is detailed in the IT Audit Section, which begins on page 61.

Audit Results

Inadequate Accounting and Administrative Controls

Adequate accounting and administrative controls help to ensure that state appropriations are spent properly and efficiently, and that funds raised through assessments, fines, and fees are appropriately collected, receipted, recorded, disbursed, and reported. The following instances of internal control weaknesses were noted.

- The Barnstable County Superior Court Clerk's Office needed to improve procedures for determining the disposition of fees paid by litigants in cases involving transfers from District Court to Superior Court. State statutes provide for final disposition of these fees under various circumstances. However, as of January 8, 2001, the Clerk's Office held \$89,669 that represented approximately 900 cases, some dating back to 1967, most of which needed to be returned to the original depositor or forwarded to the Office of the State Treasurer as abandoned property. Similar issues were disclosed relative to receivership application fees, the disposition of which is governed by Superior Court Rules. The Court Clerk responded that his staff would review the status of cases in which removal and other relevant depositor fees had been paid.
- Middlesex Probate and Family Court, at the time of this transition audit, did not have a documented internal control plan as required by Chapter 647 of the Acts of 1989, the Internal Control Statute. The lack of written administrative and accounting policies and procedures for basic court operations, such as payroll, cash receipts, and asset management, contributed to accounting and administrative control deficiencies, the specifics of which are detailed below. In addition, the Court did not have the technological resources, including computers, software, training, and direct access to the Massachusetts Management Accounting and Reporting System, to prepare proper and accurate reconciliations of expenditures and revenues.

Inadequate Accounting and Administrative Controls

(continued)

- Middlesex Probate and Family Court was not properly maintaining or accurately processing its custodial passbook records. Specifically, the Court lacked procedures for identifying passbook accounts that needed to be remitted to the State Treasurer as abandoned property in compliance with provisions of Chapter 506 of the Acts of 1990. In addition, many passbook accounts did not have either a beneficiary's Social Security number or a federal identification number as required by Internal Revenue Service regulations. Although none of the passbooks reviewed had withholding fees deducted, the bank can impose these fees whenever interest is posted to a passbook lacking proper identifying information. Finally, the Court did not have a detailed account trial balance of its custodial passbooks and, therefore, could not accurately determine their value. Because the Court did not have sufficient controls in place to ensure that custodial passbooks were properly processed and monitored, there was little assurance that these assets held in trust were adequately safeguarded or accurately reported on financial statements.
- Middlesex Probate and Family Court did not have sufficient control procedures for the collection of and accounting for funds. In addition to the custodial passbook issues noted above, bookkeeping duties were inadequately segregated; cash deposits were not always made on the day funds were received; monthly revenue balances were not reconciled with balances recorded on the Massachusetts Management Accounting and Reporting System; and monthly expenditure reports were tardy and inaccurate. These deficiencies increased the risk of loss, theft, or misuse of Court funds.
- Middlesex Probate and Family Court did not adequately document payroll expenditures. Signed individual payroll records were not maintained; supervisory oversight was inadequate; and employee compensatory time was inaccurately calculated and improperly approved. As a result, there was little assurance that all payroll expenditures were correct and proper.

Special Audit Section

- The Worcester Sheriff's Department, which was established as an independent state department in 1997, when Worcester County Government was abolished, has continued to deposit telephone revenues into its Worcester County Jail Commissary and Welfare Account. However, since the Sheriff's Department is now a state entity, it may fall under a statute requiring that these revenues be deposited in the Commonwealth's General Fund. Currently, two laws address the deposit of these revenues, one directing that the funds be forwarded to the General Fund and the other providing that they be deposited into the Commissary and Welfare Account. The OSA recommended that the Worcester Sheriff's Department obtain legal clarification to resolve the issue of which statute applies and where telephone revenues should be deposited.
- The Worcester Sheriff's Department, in accordance with state statute, provides rent-free housing for the Sheriff on the grounds of the Worcester correctional facility. During the audit period, however, the fair market value of rent and utilities was not reported as required to the Internal Revenue Service (IRS) or the Massachusetts Department of Revenue. The Sheriff's Department responded that it had received an IRS ruling that the rent waiver provided to its Sheriff was exempt from both taxes and reporting requirements. The Sheriff's Department could not document receipt of this ruling, however, and needed to obtain and place on file an official IRS statement regarding the tax status of rent, heat, and electrical service for the Sheriff's residence.

Inadequate Controls over Property and Equipment

All state entities are required to keep complete inventories of property and equipment in order to ensure that fixed assets are properly safeguarded. The following report identified areas in which inventory controls needed to be strengthened.

- Middlesex Probate and Family Court had not conducted an annual physical inventory since 1999 and did not maintain a perpetual inventory listing of property and equipment. In addition, the Court did not maintain a total value for fixed assets or reconcile its property records with the Administrative Office of the Trial Court's records of assets reported on its behalf to the State Comptroller. As a result, the Court could not be assured that its fixed assets were properly safeguarded or accurately reported on financial statements.
- The Worcester Sheriff's Department was not conducting regular and sufficient inventory checks to properly control food items and other supplies stored in its warehouse. Specifically, perpetual inventories were not maintained; the counting and distribution of food supplies were not adequately monitored; and a physical inventory of non-food supplies had not been taken in many years. As a result, the Sheriff's Department could not adequately account for, safeguard, and monitor nearly \$1.5 million in food purchases or purchases of non-food supplies. The Sheriff's Department responded by taking a physical inventory of its supplies and initiating a perpetual inventory record system.

Special Audit Section

Cooperative Investigation with the Essex County District Attorney and the State Police Regarding an Embezzlement of Funds from the Andover Police Relief Association

At the request of the Essex County District Attorney, the Office of the State Auditor assisted in the investigation of missing funds from the Andover Police Relief Association, which is a fraternal organization that provides benefits to active and retired Andover police officers and their children. OSA auditors examined the documents and records seized by the Massachusetts State Police from Kavanagh & Co., the Association's public accounting firm, whose managing partner/accountant was suspected of embezzling funds. The purpose of the audit was to determine the amount of money stolen from the Association as well as the manner of the theft. Results of this investigation follow.

- OSA audit work resulted in questioning 27 checks amounting to \$123,290 that appeared to be forgeries. These checks were all numbered beyond 1249, the last number of a sequence of checks signed by the officers of the Andover Police Department. The officers indicated that they never had custody of checks numbered from 1251 through 1501, the check register from which all the forgeries were made. At the time of the theft, blank checks were ordered from the bank by Kavanagh & Co., and delivered to the accounting firm rather than the Association. The managing partner/accountant retained a block of checks, while forwarding the rest to the Association. He then wrote checks over a two-year period, 25 of which were payable to Kavanagh & Co., and the remaining two with TP Telecom, Inc. as the payee. From records of the Secretary of the Commonwealth, it was determined that the accountant was also the Treasurer of TP Telecom at the time the checks were written.

Internal Controls over Property and Equipment

- Review of the books and records maintained for the Association by Kavanagh & Co.'s accountant disclosed that the Association was not in compliance with all Massachusetts and federal tax reporting statutes; the Association was not officially registered, as required, with the Secretary of the Commonwealth; and the Association had not ensured that its managing partner/accountant was a Certified Public Accountant.
- The State Police obtained a confession from the managing partner/accountant admitting to \$29,500 in forgeries. Subsequent to the OSA investigation, the managing partner/ accountant was prosecuted and convicted of 27 counts of forgery and larceny (i.e., theft of \$123,290). See page 77.

checks were written.

Initiatives

The following is an update on an ongoing judiciary/law enforcement initiative.

Review of Forfeited Funds/Property at District Attorneys' Offices

- The OSA will conduct a statewide audit of the forfeited funds and property received by Massachusetts District Attorneys' Offices. The audit will examine the financial records relating to forfeited funds and property. It will also evaluate compliance with applicable laws, rules, and regulations including Chapter 647 of the Acts of 1989, the Internal Control Statute. Specific objectives include a determination of the adequacy of internal controls over forfeitures and whether forfeited funds were expended and forfeited property utilized in accordance with authorized guidelines.

It is noted that deficiencies created for obstacles in reviews of these decisions by outside parties, including court and law enforcement officials.

- The Appellate Tax Board had not issued written guidelines for taxpayers appealing property valuation decisions made by local assessors or for the local entities defending against those appeals. Guidelines, at a minimum, should include a description of the appeal process, time factors affecting appeal submissions, and documentation needed in order to support an appeal. The audit did note that the Board had issued written procedures and prepared a standardized form to cover certain Department of Revenue assessment denials. However, the absence of guidelines and directives for other types of appeals, particularly local property tax valuations, denied taxpayers, local governmental entities, and other interested parties information that would facilitate their filings.

- The Appellate Tax Board's adjudicatory activities were not subject to oversight by any agency or judicial body. This lack of administrative and operational oversight contributed to the conditions described above, in which the Board made decisions impacting the expenditure of taxes without maintaining supporting documentation and without issuing appropriate guidelines. The OSA recommended legislative action to establish oversight of the Appellate Tax Board by the Department of Revenue, the Supreme Judicial Court, or some other appropriate entity.

Other Audit Reports

During the report period, the OSA issued audits pertaining to 67 various agencies, boards, commissions, and funds. Two of these reports pertained to Central Artery Project design and contract issues; two reviewed issues associated with the abolition of county government; and four reviewed Information Technology (IT) activities. These last four audits are detailed in the IT Audit Section, which begins on page 61.

Audit Results

Inadequate Accounting and Administrative Controls

Adequate accounting and administrative controls help to ensure that state appropriations are spent properly and efficiently, and that funds raised through assessments, fines, and fees are appropriately collected, recorded, and disbursed. The following reports identified areas where management and accounting controls needed improvement.

- The Appellate Tax Board did not maintain records to support its rationale in over 94% of its appeal case decisions. Most of the case files examined contained only a one-page statement that identified the parties in dispute and recorded the Board's decision. This decision statement did not provide justifying or explanatory information or incorporate any documentary evidence submitted by the appellant or the appellee. As a result of this inadequate recordkeeping, neither the taxpayer nor the taxing authority had documented information relative to the decision making process. In addition, this deficiency created serious obstacles to reviews of these decisions by outside parties, including court and law enforcement officials.
- The Appellate Tax Board had not issued written guidelines for taxpayers appealing property valuation decisions made by local assessors or for the local entities defending against these appeals. Guidelines, at a minimum, should include a description of the appeal process, time factors affecting appeal submissions, and documentation needed in order to support an appeal. The audit did note that the Board had issued written procedures and prepared a standardized form to cover certain Department of Revenue abatement denials. However, the absence of guidelines and directives for other types of appeals, particularly local property tax valuations, denied taxpayers, local government entities, and other interested parties information that would facilitate their filings.
- The Appellate Tax Board's adjudicatory activities were not subject to oversight by any agency or judicial body. This lack of administrative and operational oversight contributed to the conditions, described above, in which the Board made decisions impacting the imposition of taxes without maintaining supporting documentation and without issuing appropriate guidelines. The OSA recommended legislative action to establish oversight of the Appellate Tax Board by the Department of Revenue, the Supreme Judicial Court, or some other appropriate entity.

Inadequate Accounting and Administrative Controls (continued)

- The Board of Registration of Cosmetology did not adequately segregate licensing process duties or control data input and employee access to its licensing database. These deficiencies allowed an employee to falsify logbook entries, create unauthorized computer input forms, and issue and sell 39 fraudulent cosmetology licenses to individuals who had not met required educational and testing standards. The employee eventually pled guilty to eleven indictments, received a one-year prison sentence, paid various fines, and was ordered to perform 200 hours of community service. The audit noted, however, that contrary to Chapter 647 of the Acts of 1989, the Board did not promptly report to the OSA the sale of fraudulent licenses. The immediate reporting of any theft of funds or property is required in order to enable the OSA to examine the control environment and to recommend corrective action to prevent further fraud and misuse of funds.
- The Board of Registration of Cosmetology's Office of Investigations did not have documented procedures for conducting inspections and did not inspect licensed businesses in a timely and consistent manner. Specifically, investigations took between 25 and 645 days to complete; a significant backlog of uninspected premises existed; and many license application files did not contain the required licensing documents. As a result, some salons were operating without a license, with unsanitary conditions, or with unlicensed cosmetologists and manicurists.
- The Board of Registration of Cosmetology could not adequately document that private cosmetology schools for which it is responsible were carrying surety bond coverage. OSA testing of files of schools licensed by the Board indicated that only one of six school files contained evidence of current bond coverage. As a result, it could not be determined through Board records whether private cosmetology schools were meeting legal requirements for surety bond coverage. The audit also noted that the required bond coverage of either \$10,000 or \$20,000, depending on enrollment size, may not be sufficient to ensure that students' tuitions are protected in the event that a cosmetology school defaults on its educational commitment.

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- The Board of Registration of Cosmetology needed to appoint a seventh member and second representative of the general public in order to be fully constituted. Filling the Board's vacant position would bring its staffing into legal compliance, strengthen Board oversight, and help to ensure that the public is properly represented. In terms of compliance issues, the audit also noted that the private testing service hired by the Board to administer license examinations shredded approximately 10,300 original applications and examinations during the period July 1995 to April 1999, which was contrary to the record disposal schedule of the Commonwealth's Records Conservation Board.
 - The Division of Occupational Safety, a subdivision of the Department of Labor and Industries, notified the OSA of the possible loss of two money orders payable to the Commonwealth of Massachusetts, each in the amount of \$850. One money order had been returned to an applicant whose submitted application was incomplete. When neither the application nor the money order was received, the applicant sent a second money order, which was reported missing after being left on a desktop overnight. (Subsequently, this applicant's license was renewed, and bank reimbursement was made for the lost money orders.) Pursuant to Chapter 647 of the Acts of 1989, the Internal Control Statute, the OSA reviewed the Division's processing of license applications and safeguarding of receipts in order to assist the agency in improving its control environment. Most pertinently, the Division was not properly securing all receipts in a cash drawer or vault and was not depositing all receipts on a daily basis. Prompt deposit of receipts helps to protect them from loss or theft and maximizes interest income. The audit also noted that written guidelines did not exist for staff to report variances or loss of funds and that segregation of licensing duties was inadequate.
 - The Division of Occupational Safety did not have adequate controls over its inventory of licenses and certificates issued, and preprinted certificate control numbers were not recorded in either the Division's computer system or electronic check register. In addition, duties were not properly segregated so that the work of one employee could act as a check on that of another. As a result, the Division could not be assured that its licensing process was properly safeguarded against possible theft or misuse.
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Inadequate Accounting and Administrative Controls

(continued)

■ The Massachusetts Highway Department (MHD) permitted payroll section employees to make entries to their records that affected the amount of pay they receive. This practice, which was inadequately supervised and inconsistent with the principles of an effective internal control system, created conditions under which an employee entered into her records \$1,986.49 in bonus and other payments to which she was not entitled. Although Chapter 647 of the Acts of 1989 requires an immediate report to the OSA of loss or theft of funds, this theft, which was uncovered in July 2000, was not reported to the OSA until October 17, 2000. Furthermore, MHD did not seek a recovery of funds from the employee, who received over \$10,000 in vacation pay when she resigned in August 2000. The OSA examined the control environment in the payroll section and made recommendations for its improvement, including the immediate implementation of an appropriate segregation of payroll duties that would prohibit employees from making entries to their own payroll records. MHD responded by strengthening certain monitoring controls. However, as of the close of the audit period, a lack of segregation of duties within the payroll section remained. As a result of the audit, however, MHD did agree to seek restitution and did obtain repayment of \$1,192.94.

■ The Office of the State Treasurer, while substantially improving controls over abandoned property, was still not liquidating physical property in compliance with state law, was not properly depositing abandoned checks and currency, and was not providing adequate supervision of the staff members conducting abandoned property inventories. The Treasurer's Office responded that it is in the process of developing a comprehensive internal control plan, which will include written procedures for receiving, recording, inventorying, monitoring, safeguarding, and liquidating abandoned property.

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- The Office of the State Treasurer was still not monitoring and reconciling activities of the two banks that acted as portfolio custodians for abandoned dividends, stocks, bonds, and other intangible property. In addition, the Treasurer's Office could not provide the exact number of mutual companies that also served as custodians of abandoned property nor determine the total value of abandoned mutual funds. The OSA recommended that all abandoned intangible property, including abandoned mutual funds, be forwarded to custodian banks and that a policy be established for the recurring liquidation of stocks and bonds.
 - The Office of the State Treasurer accepted aggregate deposits of presumed abandoned property from banks and other financial institutions without the detailed information, including a name, last known address, and identifying dollar amount for each property owner required under state statute. Payments for claims made from these aggregate deposits depended solely on holders' verification, which increased their vulnerability to theft and misuse. As a result of the Office's aggregate deposit practices, over \$7 million in fraudulent abandoned property claims were authorized and paid between January and April 1999. An investigation by the Office of the Attorney General identified false claims made by General Electric Securities and Electric Data Systems Corporation based on State Street Bank and Trust aggregate filings. Subsequently, the two corporations agreed to repay \$7 million to the Commonwealth, and the Treasurer's Office suspended claim payments submitted against aggregate deposits made by State Street Bank and Trust. However, the practices described above continued to be used to pay all other claims derived from aggregate deposits.
 - The Office of the State Treasurer, during the first quarter of calendar year 2000, paid approximately \$35 million to the Internal Revenue Service (IRS) for previously underreported and unpaid federal payroll tax liabilities for 1996-1999. The audit noted that the Treasurer's Office did not have procedures in place for ensuring timely payment by the Commonwealth of its federal payroll tax obligations or for proper billing, reconciliation, and reimbursement of employer Medicare matching shares from state agencies. As a result, in addition to underpayments, for which penalties could be assessed, overpayments in excess of \$4.6 million went unrecovered for twenty months after IRS notification to the Treasurer's Office.
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Inadequate Accounting and Administrative Controls (continued)

- The Office of the State Treasurer needed to improve administration of its central disbursement account (Float Fund), management of bank service fee payments, maintenance of Commonwealth bank account listings, custodial oversight of the Eminent Domain Trust Fund Account, and custodial controls over Deposit-In-Trust Accounts. With respect to these issues, the OSA recommended review of the practice of using the Floating Fund's outstanding balance as the funding source for payments, routine monitoring of bank service fees, monthly reconciliations of trust accounts, and proper segregation of financial transaction duties.
- The Public Employee Retirement Administration Commission (PERAC) needed to increase audit coverage of the investment practices of retirement systems. During calendar year 1999, the market value of retirement system investments totaled more than \$43.8 billion, of which \$31.6 billion (72%) represented investments managed by the Pension Reserves Investment Management Board and \$12.2 billion (28%) managed by local retirement systems. Notwithstanding the significant amount of money involved, PERAC's audit activities focused on financial management by the individual retirement systems. Because PERAC's audits did not include an examination of investments, there was inadequate assurance that retirement system investments were prudent, economical, and in accordance with applicable laws and regulations. While recognizing that staff constraints affected investment audit decisions, the OSA recommended that PERAC take immediate steps to incorporate the area of investments into its audit plan. PERAC responded that it was in the process of conducting a series of targeted investment audits and taking other steps to increase oversight of the investment activity of retirement boards.
- The Public Employee Retirement Administration Commission (PERAC) was not adequately following up its audit disclosures to ensure that retirement systems were correcting deficiencies. For example, a review of findings reported by PERAC audits during the three fiscal years ended June 30, 1998 indicated that certain retirement systems' bank statements were improperly reconciled, or were unreconciled, and that variances had been allowed to accumulate for periods ranging from six months to nine years. Of sixteen systems with variances, seven had unreconciled variances of \$907,516, and the remaining nine systems demonstrated no

evidence of reconciliation. However, PERAC's work papers showed little evidence of follow-up procedures, even in those cases where recurring reconciliation problems had been disclosed. PERAC officials responded that they are now contacting all retirement boards that have been the subject of a recent audit seeking an update on corrective actions. In addition, they are publishing audit results as part of their Annual Report, which is disseminated to retirement boards, legislators, local officials, and other interested parties.

- The Public Employee Retirement Administration Commission's (PERAC) audit procedures concerning retirees' abandoned checks indicated that three retirement systems had uncashed checks on hand for extensive periods of time without attempts to resolve their ownership status. The City of Boston's retirement system, for example, had 605 uncashed checks totaling \$399,020 and was, in some instances, continuing to issue checks to individuals whose checks were already in the uncashed status. The OSA recommended that PERAC continue to work with the retirement systems to develop procedures to establish the status of those retirees who have not cashed their checks and to credit back to a retirement system's Pension Fund any payments deemed to be abandoned.

Special Audit Section: Revenue-Related Audits

Agency Compliance with Laws, Regulations, and Office of the State Comptroller Policies for Selected Transactions

The Office of the State Auditor, in conjunction with the Single Audit of the Commonwealth, conducted a review of 28 selected transactions at nine state agencies for the purpose of determining agency compliance with relevant laws and regulations. The audit also examined internal control plans and followed up on prior audit results. Except for the issues noted below, no reportable conditions were disclosed.

- The Department of Correction (DOC) and the Administrative Office of the Trial Court (AOTC) did not record all fixed assets onto the Massachusetts Management Accounting and Reporting System (MMARS) in a timely manner. DOC did not record a truck purchased in January 2000 for \$42,497 until April 2000. AOTC did not record two vehicles, one costing \$23,929 and the other \$19,520, purchased in March 1999, until September 1999, the next fiscal year. The Office of the State Comptroller's Fixed Asset Subsystem User Guide requires that assets valued at \$15,000 or more be recorded onto MMARS within seven days of acquisition in order to properly account for the state's fixed assets and accurately report their value on financial documents. The audit also noted that all fixed assets must be posted by June 30, the close of the fiscal year.
- Northern Essex Community College did not have adequate documentation for a transaction that totaled \$112,639. Although the College's Fiscal Accounting Policy and Procedures Manual states that approvals and segregation of duties should be in effect for processing nonappropriated fund activity, input of documents did not indicate who prepared, entered, or approved the transaction in question for MMARS processing. In addition, the College was not posting all financial activity on a monthly basis as required.

■ The Executive Office of Environmental Affairs had still not completed an update and expansion of its internal control plan as required by Chapter 647 of the Acts of 1989. Although the other agencies reviewed had current internal control plans, the majority of these plans needed additional emphasis on risk assessments for both financial and programmatic operations.

Special Audit Section: Revenue-Related Audits

The Department of Environmental Protection's (DEP) Community Septic Management Program

The OSA completed an audit of DEP's Community Septic Management Program's distribution of grants and loans to local communities for the repair of septic systems to meet the requirements of Title V of the State Sanitary Code. The audit also reviewed local communities' management of disbursement of these funds to homeowners. Chapter 15 of the Acts of 1996, the Open Space Bond Act, provided \$30 million in funding to DEP to administer the program in conjunction with the Water Pollution Abatement Trust. Funding is in the form of a zero-interest loan from the Trust to the local community, which must be repaid over a period of up to twenty years. Participating communities must execute a loan agreement with the Trust and issue local government bonds to secure the loan. Results of this audit, which are summarized below, indicate compliance areas in need of improvement.

- Twelve of 28 communities reviewed were not in compliance with the program requirement that they have documentation of a homeowner's failed septic system before awarding the homeowner a loan. During the audit period, however, four communities provided some documentation, such as letters from their boards of health, that systems in question were in failure. If all eligibility requirements are not adhered to, the potential exists that ineligible homeowners will receive loans while eligible applicants remain on a town's waiting list.
- Three communities entered into loan agreements with the Water Pollution Abatement Trust and then requisitioned the full amount of the loans without adequately documenting the need for those funds. Furthermore, as of March 31, 2000, these communities had expended only \$39,480 of their loan funds, leaving unspent balances totaling \$460,520. Town officials stated that regional DEP representatives instructed them to submit their requisitions for the full loan amount even though they had not obtained betterment agreements with homeowners. Because loan requisitions were approved without required supporting documentation, there was inadequate assurance that funding was awarded where it was most needed and would be used in a timely manner.

Special Audit Section: County Transfers

- Four communities did not submit quarterly reports to oversight agencies, although these submissions are a precondition for receipt of loan payments. Community officials indicated that they were not aware of the reporting requirements and that they had continued to receive funding even though they had not filed any of the required quarterly reports. Without these reports, DEP could not properly monitor the program's efficiency or communities' adherence to program guidelines. DEP responded that it was now requiring adherence to the quarterly report policy and knew of no instances subsequent to January 1999 of loan proceeds being disbursed to a community that did not meet the filing deadline.

Status of the Health Care Security Trust

The OSA reviewed the operations of the Health Care Security Trust, the repository for funds received by the Commonwealth as a result of the settlement between the tobacco industry and the Medicaid lawsuits of 46 states for recovery of tobacco-related disease costs. Massachusetts estimates its allocable share of the settlement over the next 25 years to be approximately \$7.6 billion, of which \$326,235,129 had been received as of September 30, 2000.

In accordance with the requirements of the Master Settlement Agreement, all funds received were deposited into the Health Care Security Trust Fund in the custody of the State Treasurer. The State Treasurer has been investing these funds by purchasing commercial paper investments at competitive rates ranging from 6% to almost 7%, and by depositing funds in the Massachusetts Municipal Depository Trust. In accordance with the requirements of Chapter 29D, the Office of the State Comptroller in December 1999 transferred \$91,200,000 from the Health Care Security Trust Fund into the Tobacco Settlement Fund, from which health expenditures can be made. This amount was subsequently appropriately adjusted to \$83,597,203, and the balance of \$7,602,797 was transferred back to the Health Care Security Trust. As a result, as of September 30, 2000, the balance in the Health Security Trust was \$250,867,847.

Special Audit Section: County Transfers

County Government Abolition and Transfer

Chapter 48 of the Acts of 1997 abolished Middlesex, Hampden, and Worcester counties; transferred their assets and obligations to the Commonwealth; and assigned various state agencies responsibility for former county functions. Other statutes, including Chapter 300 of the Acts of 1998 and Chapter 127 of the Acts of 1999, clarified certain transfer procedures and provided for the abolition of additional counties. Audits of all abolished counties and the transfer of their assets, liabilities, and responsibilities have been completed or are in progress. The OSA is also conducting a statewide audit of registries of deeds and is conducting or has completed audits of the sheriff's offices of the abolished counties.

During the current report period, the OSA performed an audit of the Berkshire County Transfer, The Norfolk County Registry of Deeds, and the Worcester Sheriff's Department. Results of the Sheriff's Department audit are detailed in the Judiciary/Law Enforcement Section, which begins on page 30. Results of the other two audits are detailed as follows.

- Berkshire County had not maintained a complete and centralized listing of buildings, land parcels, equipment, vehicles, and roads. Furthermore, listings maintained by individual departments were incomplete in that they did not include, or only partially included, the date of purchase, funding source, tag number, location, and purchase price. As a result, there was inadequate assurance that all former County property was properly accounted for or accurately reported on financial documents. The audit also noted that county abolition legislation needed to be amended to require that all former county real property be recorded and filed in the appropriate registry of deeds to indicate ownership by the Commonwealth.
- Although there were no provisions for severance packages within the County's personnel policies, all nine employees who did not transfer to positions within the Commonwealth received severance packages, which cost a total of \$74,354. There was also a lack of documentation, such as adequate attendance/leave records to support individual severance packages, which ranged between \$1,000 and \$10,000. Payment of these severance packages reduced the amount of money available to pay Berkshire County bills, resulting in the transfer of additional liabilities to the Commonwealth.

Status of the Transfer of Berkshire County Functions, Assets, and Liabilities to the Commonwealth

The OSA review determined that the transfer of critical functions and duties was effectively carried out by the Executive Office for Administration and Finance and other parties mandated to complete the transition. Specifically, 168 former county employees were officially transferred to state payrolls as required. These former county employees were also incorporated into the Group Insurance Commission and the state retirement system. However, several issues were identified that were still pending resolution, as discussed below.

- Although all Berkshire County revenue should have been transferred to the Commonwealth as of July 1, 2000, the County Treasurer continued to receive bank statements for six active bank accounts in the County's name. These accounts and their related balances, totaling more than \$313,972, still had not been officially transferred to the Commonwealth as of February 28, 2001.
- Berkshire County had not maintained a complete and centralized listing of buildings, land parcels, equipment, vehicles, and roads. Furthermore, listings maintained by individual departments were incomplete in that they did not include, or only partially included, the date of purchase, funding source, tag number, location, and purchase price. As a result, there was inadequate assurance that all former County property was properly accounted for or accurately reported on financial documents. The audit also noted that county abolition legislation needed to be amended to require that all former county real property be recorded and filed at the appropriate registry of deeds to indicate ownership by the Commonwealth.
- Although there were no provisions for severance packages within the County's personnel policies, all nine employees who did not transfer to positions within the Commonwealth received severance packages, which cost a total of \$74,254. There was also a lack of documentation, such as adequate attendance/leave records to support individual severance packages, which ranged between \$1,000 and \$19,320. Payment of these severance packages reduced the amount of money available to pay Berkshire County bills, resulting in the transfer of additional liabilities to the Commonwealth.

Norfolk County Registry of Deeds: Transition Audit

All Massachusetts registries of deeds, including those situated in counties that have not been abolished, have been placed under the authority of the Office of the Secretary of State. During the report period, the OSA, at the request of the newly elected Register of Deeds, conducted an audit of the revenues collected by the Registry as of January 3, 2001 and the disbursement of those revenues to Norfolk County and the Massachusetts Department of Revenue. This review indicated that the Norfolk County Registry of Deeds properly collected, reported, and deposited \$3,054,626 as of January 3, 2001 and disbursed funds in compliance with applicable laws, rules, and regulations. The review also disclosed that newly implemented internal controls in place at the time of transition were adequate.

Special Audit Section: Central Artery/Tunnel (CA/T) Project

CA/T Project Oversight Coordination Commission

The CA/T Project Oversight Coordination Commission, which was created pursuant to provisions of Section 2B of Chapter 205 of the Acts of 1996, represents a unified effort to prevent or detect and correct waste, fraud, and abuse at the Central Artery Project. The Commission, made up of the offices of the State Auditor, the Inspector General, and the Attorney General, is charged with combining the expertise and statutory authority of these offices in order to target management difficulties, to identify cost-saving measures, and to pursue enforcement and recoupment actions where appropriate.

In the time period covered by this Semi-Annual Report, the OSA issued three reports relative to the CA/T Project. One audit, which reviewed proposed contract changes affecting the East Boston portion of the Project, contained no reportable conditions. Results of the other two reviews are detailed below.

- Berkshire County had not maintained a complete and centralized listing of buildings, land parcels, equipment, vehicles, and roads. Furthermore, listings maintained by individual departments were incomplete in that they did not include, or only partially included, the date of purchase, funding source, tag number, location, and purchase price. As a result, there was inadequate assurance that all former County property was properly accounted for or accurately reported on financial documents. The audit also noted that county abolition legislation needed to be amended to require that all former county real property be recorded and filed at the appropriate registry of deeds to indicate ownership by the Commonwealth.
- Although there were no provisions for severance packages within the County's personnel policies, all nine employees who did not transfer to positions within the Commonwealth received severance packages, which cost a total of \$74,254. There was also a lack of documentation, such as adequate attendance/leave records to support individual severance packages, which ranged between \$1,000 and \$19,320. Payment of these severance packages reduced the amount of money available to pay Berkshire County bills, resulting in the transfer of additional liabilities to the Commonwealth.

Prior Audit Results: Corrective Actions

CA/T Project Insurance Program

Wrap-up insurance programs, which are created by contract between the insured and the insurance carrier, provide coverage for a variety of risks. The CA/T's wrap-up program, for example, included coverage for workers' compensation and general liability. In two prior audits, the OSA examined financial aspects of the CA/T's insurance program. The current audit reviewed selected management controls, including contractual documentation.

- CA/T Project's wrap-up insurance contract agreements covering major provisions of its workers' compensation and general liability coverage were unsigned or had remained unsigned for lengthy periods of time. This procedure was contrary to state statute, CA/T's established accounting policies, and sound business practice.

Commission

Special Audit Section: Central Artery/Tunnel (CA/T) Project

The Massachusetts Turnpike Authority's Oversight Activities Relative to the North/South Rail Link in Boston

The metropolitan Boston area is currently served by a local and regional passenger rail service that is divided into separate and independent rail systems, one terminating at North Station and the other terminating at South Station. There is no direct rail link connecting North and South stations, which are approximately one mile apart. In order to address the inconvenience this causes many passengers and to encourage expanded use of public transportation to and through Boston, the North/South Rail Link project would build an underground railroad connection between North and South stations in the same corridor as the new depressed Central Artery. To date such a connection has not been built and, given the expense of the project and still unresolved engineering and construction issues, is not expected to be undertaken in the near future. The audit examined CA/T Project's management activities associated with the design and construction of the North/South Rail Link through December 31, 2000.

- CA/T Project management did not resolve, in a timely manner, a project design issue regarding the tunneling method to be used in the construction of the North/South Rail Link. Instead, the Massachusetts Highway Department pursued dual design and construction activities for a period of twenty months, which resulted in approximately \$4.5 million in unnecessary design and construction costs.
- CA/T Project expended approximately \$6.9 million in state highway funds for design and other activities associated with the North/South Rail Link, which is not a highway project. The audit recommended that CA/T Project management seek reimbursement from the MBTA of funds expended on rail link activities. The CA/T Project Director responded that although preserving the potential for future construction of a rail link was a CA/T Project environmental commitment as well as a goal of the Executive Office of Transportation and Construction, which is the umbrella entity of the Commonwealth's transportation agencies, he would forward the OSA recommendation to MBTA management. The OSA noted, in further response, that the Secretary of Environmental Affairs's Certificate on the Final Supplemental Environmental Report specifically excluded the North/South Rail Link as an environmental mitigation requirement.

Prior Audit Results: Corrective Actions

A review of prior audits is an important component of each OSA audit. This follow-up review helps to monitor and acknowledge agency compliance with OSA recommendations. Corrective actions, based on OSA recommendations, were taken by the following entities.

Department of Correction (DOC)

- DOC, as noted in the OSA's Statewide Test of Transactions, has improved the accuracy of its applications for reimbursement from the U.S. Bureau of Justice Administration for the State Criminal Alien Assistance Program.

Office of the State Treasurer

- The Office has strengthened controls over abandoned tangible property held in its vault and improved procedures for notifying abandoned property owners.
- The Office has hired a new Director of Auditing and Compliance to review, monitor, and improve procedures for identifying abandoned property not transferred by holders to the Commonwealth in accordance with state law.

Metropolitan District Commission (MDC)

- MDC has developed written policies and procedures to address the inventory of its motor vehicles and has reconciled its inventory records with information on the Massachusetts Management Accounting and Reporting System, and at the Registry of Motor Vehicles.

Initiatives

The following are among planned and ongoing initiatives relative to various state agencies and programs.

Depression of the Central Artery/Third Harbor Tunnel

- The OSA is reviewing and assessing the system of internal controls that the Massachusetts Highway Department and the Massachusetts Turnpike Authority have established for estimating, monitoring, and controlling project costs in order to identify system weaknesses and opportunities for savings; cost avoidance; and adherence to timing, scheduling, and performance requirements. This audit will result in a series of reports, fifteen of which have been issued.

Massachusetts Highway Department (MHD)

- The OSA is conducting a review of MHD's Road and Bridge Program to determine whether it is being adequately funded. The audit will, for example, examine expenditures on road and bridge projects to determine whether the Commonwealth is complying with the federal requirement that 29% of its annual federal highway funding be allocated to projects other than the Central Artery/Third Harbor Tunnel.

Massachusetts Highway Department (MHD)- Snow and Ice Removal

- The OSA is conducting an audit pursuant to Section 331 of Chapter 127 of the Acts of 1999, which requires the State Auditor's Office to prepare a report on the expenditure of funds for the removal of snow and ice. The report will include, but not be limited to, an analysis of the adequacy of current controls on the expenditure of such funds, the appropriateness of departmental standards for the activation of contractors, measures taken to prevent fraud and abuse in the program, and measures taken to control overtime compensation costs.

Review of Revenue Processing by Registry of Deeds Offices

- The OSA is conducting a statewide audit of revenue processing by registry of deeds offices in the Commonwealth. The review will identify all sources of fees and revenues and determine whether formal, written policies exist regarding the collection, accounting, and depositing of said fees and revenues. Internal controls over fees and revenues will also be reviewed to determine their adequacy.

Review of Retirement Boards

- The OSA is conducting an audit to review and analyze various Retirement Boards' internal controls over administrative and operating costs. The audit will include, but not be limited to, a review of administrative costs such as travel, consultants, conferences, and employee use of credit cards to determine whether these costs are appropriate, reasonable, and allowable. It will also review compliance with all applicable laws, rules, and regulations and the adequacy of internal controls over said costs.

Single Audit of the Commonwealth

- During fiscal year 2002, the OSA will once again be a partner in performing the "Single Audit of the Commonwealth," a comprehensive annual audit of the Commonwealth as a whole that encompasses the accounts and activities of all state agencies. This audit satisfies the federal and state requirements to audit the Commonwealth of Massachusetts' financial operations consisting of its accounts, programs, activities, funds, and functions, as well as specified compliance issues.
- As a partner in the "Single Audit," the OSA will also provide staff resources for the audit of federal programs to determine whether the state is in compliance with applicable federal laws, rules, and regulations. The OSA will conduct audit procedures that are needed to render an opinion on the Commonwealth's Comprehensive Annual Financial Report.
- The OSA will also participate substantively in the "Single Audit of the MBTA" by testing certain capital and operating expenditures to determine the MBTA's compliance with various federal requirements. In addition, the OSA will continue to assist housing authorities and other entities in meeting their responsibilities under the Federal Single Audit Act.

Initiatives

- In addition to the reports listed in the Appendix on page 94, the following reports are issued annually in compliance with state and federal laws and regulations:

Statutory Basis Financial Report

Comprehensive Annual Financial Report

Report on Compliance and Internal Control in Accordance with Government Auditing Standards

Report on the Requirements of OMB Circular A-133

Report on the Schedule of Expenditures of Federal Awards

Statewide Review of the Commonwealth's HR/CMS Payroll System

- The OSA is conducting an audit of the Commonwealth's new payroll system, HR/CMS, to determine whether there are adequate internal controls within the system and at the agency level to safeguard state payrolls. The audit will examine compliance with the Comptroller's Payroll Manual, the HR/CMS Manual, and other applicable criteria.

Statewide Review of Fees for Services

- The OSA is conducting an audit to determine whether the fees charged by state agencies for various services, permits, licenses, and inspections are set at the amounts mandated by state laws and regulations. The audit will also determine the monetary effect to the Commonwealth of any identified instances of noncompliance.

Review of Revenue Processing by Registry of Deeds Offices

The OSA is conducting a statewide audit of revenue processing by registry of deeds offices in the Commonwealth. The review will identify all sources of fees and revenues and determine whether formal, written policies exist regarding the collection, accounting, and depositing of said fees and revenues. Internal controls over fees and revenues will also be reviewed to determine their adequacy.

Information Technology Audits

During the report period, the OSA's Information Technology (IT) Audit Division issued eight audit reports and two management letter reports detailing strengths and weaknesses of internal controls within IT-related and certain financial-related areas. In addition, in response to the changing information technology environment throughout the Commonwealth, the IT Audit Division has continued to update survey information pertaining to IT-related operations. Using survey and pre-audit information, the Division initiates audit engagements based upon technological importance and levels of risk to agency data centers or automated systems.

Information technology auditing is the process of collecting and evaluating evidence to determine whether computer systems or technology environments are sufficiently controlled to provide reasonable assurance to adequately safeguard assets, maintain data and system integrity, achieve organizational goals effectively, and consume resources efficiently. The IT Audit Division conducts general and application internal control examinations that provide independent, objective appraisal of the adequacy of internal controls over and within information systems and IT processing facilities. Information technology auditing also includes providing technical support to financial and performance auditors in evaluating IT-related or information systems-related controls and retrieving selected information from automated systems.

Audit Results

The primary audit responsibility of the IT Audit Division is to conduct internal control examinations of the Commonwealth's automated systems and IT processing environments. The objective is to determine whether sufficient controls are in effect to provide reasonable assurance that automated systems can be relied upon and that processing can be performed in an accurate, complete, valid, and timely manner. Audit objectives for information systems may include determining whether adequate controls are in place to provide reasonable assurance that control objectives regarding security, integrity, and availability will be met. This Division also examines financial-related controls, which are generally reported in integrated IT and financial audits. Audit results warranting management attention recorded during this report period disclosed issues in a number of areas, including disaster recovery and business continuity planning, environmental protection and physical security, system access security, and accounting, administrative, and inventory controls.

Disaster Recovery and Business Continuity Planning

The overall objective of disaster recovery and business continuity planning is to provide reasonable assurance that mission-critical or essential computer operations can be restored within acceptable periods of time in the event of significant disruptions or loss of processing capabilities. Other contingency planning objectives are to safeguard data, programmed software, and critical documentation; to ensure employee safety; to minimize security exposures and system damage; and to reduce the time required to recover from system disruptions or failure.

- The Board of Registration in Medicine needed a more comprehensive business continuity strategy to ensure resumption of mission-critical processing within an acceptable time frame should automated systems be rendered inoperable or inaccessible. Essentially, more detail was needed in the recovery plan and, in particular, with regard to source document management. Specifically, the Board had not formally designated an alternate-processing site, performed a formal walk-through of the plans, or conducted disaster recovery tests to assess the feasibility of the plans. The audit did note that backup copies of transaction and master files and software programs were maintained at secure on-site and off-site locations. However, until the business continuity plans are more thoroughly developed, reviewed, and tested, the Board lacks adequate assurance as to the viability of its recovery strategies.

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- The Group Insurance Commission (GIC), while following sufficient backup procedures, had not developed a formal, tested business continuity plan for the timely restoration of mission-critical and essential business functions to be used in the event that automated systems are rendered inoperable or inaccessible. Without sufficient business continuity planning, including a viable alternate processing site, a possible long-term loss of GIC's computer operations could hinder access to information regarding participants' eligibility for insurance programs, as well as the processing of health, life, and other insurance benefits for participants in GIC programs. The OSA recommended that GIC perform a risk analysis and criticality assessment, and then develop appropriate policies and strategies for alternate-site processing and restoration of critical business functions.
 - The Massachusetts Correctional Institution at Cedar Junction still needed to formalize and test its draft business continuity plan. The audit noted that the draft plan outlined a sound strategy for maintaining system availability in the event of a major disaster or disruption of IT operations and that adequate procedures were in place regarding the production of backup copies for on-site and off-site storage of computer-related media. Prison official responded that they would test, review, and routinely update their business continuity plan, as recommended.
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Audit Results

Disaster Recovery and Business Continuity Planning (continued)

■ The Massachusetts Highway Department (MHD) did not have a documented business continuity plan to provide for the timely restoration of mission-critical and essential business functions should automated systems be rendered inoperable or inaccessible. In addition, although certain backup procedures were being performed, an alternate-processing site had not been designated. MHD officials responded by initiating a written business continuity plan while the audit was in progress. At the close of the audit period, MHD still needed to perform a risk analysis, then fully develop and test plans and procedures for alternate-site processing and restoration of systems operations.

■ The Soldiers' Home in Holyoke had not developed a formal, comprehensive business continuity plan for restoring processing functions in the event that automated systems were rendered inoperable or inaccessible. This deficiency, which was identified in a prior review, resulted in significant disruptions to third-party billing operations, primarily because no viable alternative method of processing was in place when the Soldiers' Home's primary administrative system failed to operate from August 1998 through December 1999. In the absence of a written plan based on the results of a risk analysis and criticality assessment and sufficient testing of the recovery strategies, the Soldiers Home continued to be vulnerable to failures in its billing system, as well to the loss of other essential data processing and business functions, should a disaster occur.

■ The Board of Registration in Medicine needed a more comprehensive business continuity strategy to ensure resumption of mission-critical processing within an acceptable time frame should automated systems be rendered inoperable or inaccessible. Essentially, more detail was needed in the recovery plan and, in particular, with regard to source document management. Specifically, the Board had not formally designated an alternate-processing site, performed a formal walk-through of the plans, or conducted disaster recovery tests to assess the feasibility of the plans. The audit did note that backup copies of transaction and master files and software programs were maintained at secure on-site and off-site locations. However, until the business continuity plans are more thoroughly developed, reviewed, and tested, the Board lacks adequate assurance as to the viability of its recovery strategies.

Environmental Protection Controls and Physical Security

Proper environmental protection and physical security for data centers and on-site or off-site media storage rooms serve to minimize significant risks regarding staff safety and damage to, or destruction of, the physical plant, equipment, data, and software. In addition, adequate physical security serves to minimize the risk of unauthorized persons breaching security and gaining unauthorized entry to areas housing valuable computer-related equipment and information.

- Greenfield Community College needed to improve certain environmental protection and security controls. Specifically, installation of water detectors in both the academic and administrative data centers and elevating the file servers in the academic data center would reduce risks of water damage. In addition, electrical appliances, such as a microwave oven, toaster oven, and refrigerator should be removed from the computer room, and emergency lighting should be installed. The OSA also recommended strengthening fire protections and posting emergency procedures for the administrative and academic data centers.
- The Massachusetts Highway Department (MHD) needed to improve physical security and environmental protection over on-site and off-site storage for critical and important data files and software. Specifically, backup tapes stored in a manager's desk at the central office needed to be moved to a secure location. With respect to off-site storage, certain backup tapes were kept at a manager's home, contrary to MHD's own guidelines for secure media storage and sound computer industry practices. In addition, the room used for off-site storage in Boston was not properly locked and also functioned as an electrical closet and communications room. Backup tapes were stored in cardboard boxes and, in certain instances, within three feet of major electrical connections. As a result, MHD could not be assured that its backup tapes were properly safeguarded from unauthorized use, damage or erasure by magnetic fields produced by electrical cables, or possible electrical fire.

Inventory Controls: IT-Related Assets

All state entities are required to keep complete inventories of IT resources, such as computer equipment and software, to ensure that these fixed assets are properly safeguarded, accounted for, and used for the purposes intended. In addition, with respect to software, inventory records and periodic tests should be used to help prevent unnecessary software expenditures, software copyright infringement, and loss or theft of software products. Prevention of the unauthorized installation and use of software also decreases the risk of importing viruses, helps to ensure the integrity of data files, and protects agencies and individuals from the risk of legal action for copyright infringement.

- The Cambridge Housing Authority, while taking steps to substantially improve inventory controls, had not conducted a physical inventory and reconciliation of inventory records for fiscal year 2000. The Authority also needed to more closely monitor the work of the contractor hired to convert from an old accounting system to a new integrated accounting information system, which included a fixed-asset inventory module that can assist in maintaining a perpetual inventory record. As of the end of audit fieldwork, the inventory list generated by the new system contained items that had been disposed of or were not found in the location recorded in the data file. The Authority responded that additional work by the contractor was in progress and would correct the systems problems noted. Also, an annual physical inventory was also planned for fiscal year 2001.
- Greenfield Community College had not tagged all computer equipment nor updated the location designation for 577 IT-related items on its inventory record. In addition, the Computer Services Department maintained a hardware inventory record separate from and not reconciled with the College's master inventory. As a result, a number of items were found in locations other than those listed on the inventory record, and the integrity of the unreconciled listing could not be assured. Regarding software, the College needed to establish a policy and procedure whereby microcomputers would be routinely checked for unauthorized or potentially illegal software.

Financial-Related Issues

- The Massachusetts Highway Department (MHD) did not maintain a current, accurate, and complete inventory record to properly account for IT-related assets. For example, inventory records did not include all necessary information regarding cost, date of acquisition, or time of last update of hardware, and did not include software at all. In addition, MHD could not document that an annual physical inventory and reconciliation of IT-related assets had been performed. Finally, MHD incorrectly computed some of the historical costs that were entered into inventory records and did not properly enter information into the Massachusetts Management Accounting and Reporting Fixed Assets Subsystem. As a result, MHD officials placed IT-related assets, valued in excess of \$15 million, at risk of loss, theft, or misuse and reported inaccurate and incomplete information on financial documents filed with the Office of the State Comptroller.
- The Soldiers' Home in Holyoke could not provide an up-to-date, accurate, and complete inventory record for all software. As a result, the Soldiers' Home could not be assured that software products residing on microcomputers were properly accounted for or that controls were sufficient to prevent and detect unauthorized use or copying of software.

System Access Security

Industry guidelines and baseline controls advocate that appropriate access security controls be in place for mission-critical or high-risk systems to ensure that only authorized personnel obtain system access. Access to automated systems should be granted on a need to know, perform, and protect basis. Written policies and procedures for access security administration should be in place to provide operational rules and guidelines for the security of informational assets and to ensure that appropriate and prompt actions are taken to review unauthorized access attempts. Without system access restrictions, such as the periodic changing or deactivating of passwords and user IDs for individuals no longer requiring or authorized to have access, unauthorized access could be gained, resulting in the risk of system data and programs being disclosed, damaged, deleted, or modified.

- Greenfield Community College did not have sufficient procedures in place to ensure notification to its Computer Service Department's security administrator of changes in employment status of staff who had been granted access to information systems. Consequently, active user accounts existed for many individuals no longer employed at the College. In addition, passwords were not periodically changed, further increasing the risk of unauthorized access to automated systems. These deficiencies increased the vulnerability of critical information on the College's systems to unauthorized access, alterations, and deletions.
- The Massachusetts Highway Department (MHD) needed to strengthen certain access security controls to ensure that user IDs and passwords would be active for only authorized personnel and to ensure timely action in closing user accounts. The audit noted some active user IDs for individuals who were no longer employed by the Department. In addition, the majority of employees did not have access authorization forms on file. Without such forms, MHD could not readily verify or confirm levels of access privileges granted. MHD responded by disabling all user accounts identified during the audit as no longer valid and initiating other corrective actions, such as securing contractor users' logon privileges with a start and end date.

Special Audit Section: Selected Management Financial-Related Issues

Inadequate Accounting and Administrative Controls

Adequate accounting and administrative controls assist entities in maximizing revenue potential and minimizing vulnerabilities to waste, lost income, and lost property. The following instances of administrative and internal control weaknesses were noted.

- The Board of Registration in Medicine did not properly report to the OSA a missing laptop computer, contrary to the provisions of Chapter 647 of the Acts of 1989, the Internal Control Statute. The immediate reporting of any loss or theft of funds or property is required in order to enable the OSA to examine the control environment and recommend corrective action to prevent further unauthorized use or loss of assets. The Board responded by reporting the missing laptop while audit fieldwork was still in progress and by reviewing with IT staff the proper procedures for reporting lost or stolen equipment.
- Greenfield Community College could not provide written contracts for two IT-related service contracts that together cost \$73,000. Although nothing came to the OSA's attention to indicate that services were not provided, having contracts and documentation of contracted services readily on hand provides an effective mechanism for monitoring contract performance and ensuring that all terms and conditions are met. The audit also noted that, prior to the audit period, the College, contrary to its own internal control procedures and those required by Chapter 647 of the Acts of 1989, did not report to the OSA the theft of a video camera with an approximate value of \$3,000. The College recognized that IT management and staff had been insufficiently aware of Chapter 647 reporting requirements and took steps to address this issue and to strengthen internal controls in general.

Inadequate Accounting and Administrative Controls (continued)

- The Soldiers' Home in Holyoke had serious deficiencies in its billing and accounts receivable operations, especially between September 1998 and December 1999, when its mainframe computer failed. Although the Soldiers' Home attempted to manually process third-party billings during part of this period, it was only able to process less than two percent of the total bills receivable. As a result, approximately \$2 million of patient billings were not processed for at least sixteen months. At the close of the audit period in May 2001, the Soldiers' Home was still working to reduce its billing backlog. As noted in the earlier discussion of business continuity planning, the Soldiers' Home did not have adequate contingency plans and, consequently, could not implement alternative billing-processing methods in a timely manner.

Special Audit Section: Selected Management Letters

The following section summarizes general findings and recommendations from two management letters issued during the current report period.

The Bureau of State Office Buildings

The OSA performed a security review of the communication and electrical closets of the state buildings under the control of the Bureau of State Office Buildings. The purpose of the review was to determine whether closets housing critical data and voice communication or electrical lines had sufficient controls to prevent and detect unauthorized access and accidental or malicious damage. Among other issues, the review disclosed concerns regarding the management of access keys to the closets at many state buildings and made several recommendations, as detailed below.

- The Bureau of State Office Buildings did not have a master list of keys or individuals assigned keys, did not have a consistent key assignment policy, and did not have formal procedures to ensure timely retrieval of keys from employees and contractors no longer authorized to access communication and electrical closets. In addition, there was no policy requiring that closets be locked when unattended. The review noted open and unattended closets, closets being used as storage space, and closets containing flammable materials. These deficiencies, if not corrected, could place at risk state assets, agency operations, and the privacy and confidentiality of the state's information.
- The OSA recommended that the Bureau of State Office Buildings conduct a risk analysis and vulnerability assessment of all communication and electrical closets within buildings under its control. Based on results of these studies, a master security plan addressing access, environmental controls, and violation follow-up should be developed and implemented. Bureau officials indicated that corrective action would be taken.

Roxbury Community College

The OSA performed a review of documentation concerning a request to Roxbury Community College by a private vendor, Campus Works, Inc., for reimbursement from the College for certain contracted services start-up costs. The purpose of the review was to provide College officials with a baseline summary of matters important to consider in decisions regarding the payments in question. Results of this review follow.

- The OSA identified certain charges as clearly questionable in that they did not directly benefit the College's operations or otherwise did not comply with guidelines used by the Commonwealth to support authorization of payment. These questionable expenses included charges for meals, cellular phone usage, automobile rentals, air travel, dry cleaning services, and computer-related equipment that was not subsequently turned over to the College. In addition, the review noted billings for charges that had already been paid by another state entity and requests for reimbursement that were not fully supported by receipts.
- The OSA stated, in conclusion, that since the College had agreed upon contract addendum to reimburse the contractor for start-up costs, including expenses necessary for travel, lodging, and relocation, requests for reimbursement deemed appropriate and allowable should be paid. However, those requests that are not start-up costs or that have been identified as excessive, of a personal nature, or inadequately documented should not be authorized for payment. The management letter includes an appendix with information detailing specific charges that require scrutiny by senior College administrators.

Investigations Pursuant to the Internal Control

Prior Audit Results: Corrective Actions

Massachusetts Highway Department (MHD)

A review of prior audit results is an important component of each OSA audit. This follow-up review helps to monitor and to recognize agency compliance with OSA recommendations. Corrective actions, based on OSA recommendations, were taken by the following entities.

Cambridge Housing Authority

- The Authority has developed and implemented a documented business plan that is comprehensive and includes adequate procedures for the storage of on-site backup computer media.

The Massachusetts Highway Department (MHD)

- MHD has improved physical security and environmental controls, particularly at its central office and Arlington district office.

- The OSA recommended that MHD take immediate action to ensure an acceptable separation of duties within its payroll operations. One possibility would be to entrust payroll records for payroll action employees to the Director of Payroll or some other appropriate manager. MHD responded by strengthening certain monitoring controls. The agency also agreed to seek restitution and did obtain repayment of \$1,192.00. However, a lack of segregation of duties within the payroll sector remained.

Enforcement Assurance

In carrying out its responsibility to help ensure compliance with state and federal law, the OSA refers audits that disclose serious possible violations of law to enforcement authorities, including the Office of the Attorney General and various District Attorney's Offices. In addition, the OSA responds to specific requests to assess the control environment at agencies where thefts or shortages have occurred and to confirm the amount of funds missing. Enforcement activities during this report period are detailed below.

Investigations Pursuant to the Internal Control Statute

Massachusetts Highway Department (MHD)

- Pursuant to the requirements of Chapter 647 of the Acts of 1989, MHD's Director of Administrative Services reported a theft of funds through the agency's payroll system. The Chapter 647 report described a theft of \$1,986.49 by a payroll section employee, who made unauthorized entries to her payroll records during June and July 2000. The OSA, in initiating its review of the control environment in which the theft took place, noted that MHD did not immediately report the theft, as required, and did not attempt to recover the diverted funds. The completed review identified internal control policies and procedures in need of modification and made recommendations to correct control weaknesses.
- The OSA review disclosed that payroll section employees had access to all pay records, including their own, and were permitted to make entries to their records that affected the amount of pay they received. This practice, wherein segregation of duties within the payroll section was essentially absent, was inconsistent with effective internal control procedures and created the conditions that allowed the theft to occur. The audit also noted that inadequate supervision further compromised the control environment.
- The OSA recommended that MHD take immediate action to ensure an acceptable separation of duties within its payroll operations. One possibility would be to entrust payroll records for payroll section employees to the Director of Payroll or some other appropriate manager. MHD responded by strengthening certain monitoring controls. The agency also agreed to seek restitution and did obtain repayment of \$1,192.94. However, a lack of segregation of duties within the payroll section remained.

University of Massachusetts at Amherst: Procurement Credit Card (Procard) Program

- Pursuant to the requirements of Chapter 647 of the Acts of 1989, University officials filed a report with the OSA that identified the inappropriate use of Procard Program credit cards by a Theater Department employee. Theater Department officials had notified the University's Procurement Office of concerns involving the accountability of its Procard credit cards. This resulted in the freezing of nine credit cards and further review by the University's Internal Audit Division, which identified improper charges for purchases of electronic equipment, clothing, lodgings, and liquor by a department employee. The OSA noted in its review that the University did not immediately report the suspected improper credit card charges, as required under Chapter 647 in order to promote prompt corrective action. The OSA identified internal control weaknesses that increased the vulnerability of the Procard Program to theft and misuse of funds and made recommendations to correct the conditions found.
- The OSA review disclosed that an inadequate segregation of duties, which allowed the Theater Department employee to be both a Procard Program cardholder and the department's Records Manager, allowed him to circumvent controls that were in place.
- The OSA recommended the immediate provision for adequate segregation of Procard Program duties so that oversight and monitoring at the department level is done by officials who do not have use of Procard cards. The OSA also recommended that the University consider limiting Procard usage to employees directly involved in procurement operations. Finally, the University needed to review its employment termination process to ensure that notification is sent promptly to the payroll department. Although the employee in question repaid \$3,202 in improper Procard purchases, as well as \$376 in misused petty cash, he was overpaid \$165.81 because the Payroll Department did not receive timely notification of his termination date.

Joint Investigation

Andover Police Relief Association

At the request of the Essex County District Attorney, the OSA assisted in the investigation of missing funds from the Andover Police Relief Association. OSA auditors examined documents and records seized by the State Police from the Association's public accounting firm, Kavanagh & Co., because an accountant/managing partner in the firm was suspected of embezzling funds. The OSA determined that \$123,290 was embezzled from the Association over a two-year period. The State Police had obtained a confession from the managing partner admitting to \$29,500 in forgeries. Subsequent to the OSA investigation and documentation of the manner of the theft, the accountant/managing partner was indicted and convicted of embezzling \$123,290. In January 2001, he made full restitution and was sentenced to 90 days imprisonment and one year probation.

Division of Local Mandates

The Division of Local Mandates (DLM) was established by Proposition 2 ½ to determine the financial impact on cities and towns of proposed or existing state laws and regulations. Section 27C of Chapter 29 of the General Laws generally provides that any post-1980 law or regulation imposing service or cost obligations on cities, towns, regional school districts, or educational collaboratives shall be effective only if locally accepted or fully funded by the Commonwealth. Any protected party aggrieved by such a law or regulation may petition Superior Court to be exempted from compliance until the necessary state funding is provided. DLM's determination of the cost imposed may be offered as prima facie evidence of the state funding necessary to sustain the mandate.

DLM maintains a Legislative Review Program to analyze pending legislation on mandate-related issues. To ensure that the local cost impact of legislation is considered by the General Court, DLM reviews thousands of bills, prepares preliminary cost studies, and contacts members of the Legislature to make them aware of the Auditor's concerns. In addition, DLM responds to requests from individual legislators, legislative committees, municipalities, and governmental associations.

Mandate Determinations and Legislative Studies

Chapter 126 of the Acts of 1984 expanded DLM's powers of review by authorizing DLM to examine any state law or regulation that has a significant local cost impact, regardless of whether it satisfies the more technical standards for a mandate determination. This statute is codified as section 6B of Chapter 11 of the General Laws. Chapter 126 reviews include cost-benefit analyses and recommendations to the General Court.

Through these functions, DLM works to ensure that state policy is responsive to local fiscal realities, so that cities and towns can maintain autonomy in setting municipal budget priorities.

The following section highlights samples of this work during the reporting period.

Mandate Determinations and Legislative Studies

Chapter 139 of the Acts of 2000: Beaver Control

In response to a request from Senator Stephen Brewer, Auditor DeNucci issued an opinion that costs imposed on municipal boards of health by Chapter 139 of the Acts of 2000 are subject to the provisions of the Local Mandate Law.

Chapter 139 transfers much of the responsibility for approving applications to remediate flooding caused by beaver activity from state government to local boards of health. Prior to issuing a permit, a board of health representative must determine whether beaver activity poses a threat to human health or safety and issue emergency permits to alleviate such threats through trapping, dam breaching, or other flow control measures.

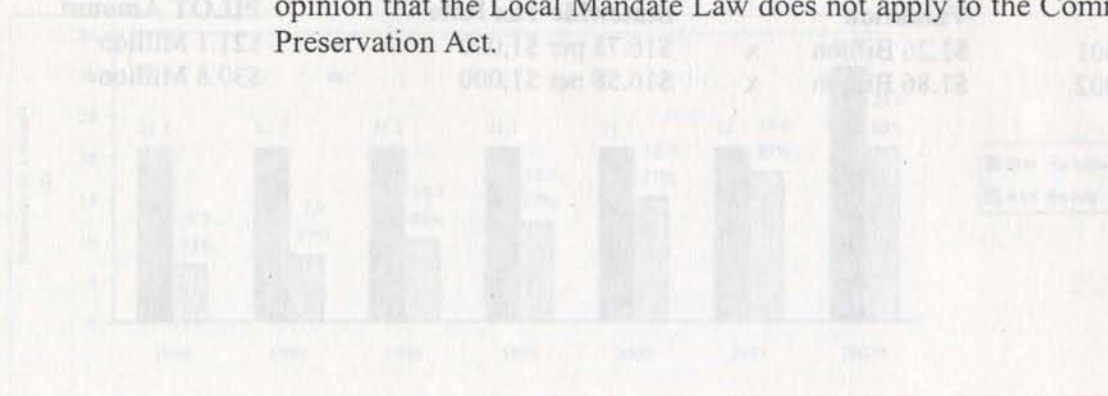
The intent of local permitting is to improve the timeliness of the response to dangerous and unhealthy flooding caused by both beavers and muskrats. However, the increased responsiveness expected from permitting by local health boards imposes a new mandate for which state funding should be provided to cities and towns.

After consulting with the Division of Fisheries and Wildlife and the Massachusetts Health Association, DLM estimated that the cost per permit issued would be \$200. Towns with elected health board members, but without paid staff, should also be eligible for state funding. These towns may need consultants or assistance from regional health agents or municipal animal control officers. DLM recommended an appropriation of \$200,000 to compensate health boards for investigating up to 1,000 complaints, and to issue permits where appropriate.

Recording Fees at Registries of Deeds: Community Preservation Act Requests

At the request of the Town of Oxford's Treasurer, DLM issued an opinion that the Local Mandate Law is not applicable to a provision of the Community Preservation Act (Chapter 267 of the Acts of 2000) that adds a surcharge to recording fees at registries of deeds.

Cities and towns, as well as all other parties leaving documents for recording at registries of deeds, have been obliged to pay fees charged by the registrars, including fee increases, at least since the 1920s. Section 2 of the Community Preservation Act is part of the series of amendments to Section 38 of Chapter 262, MGLs, that have increased registry recording fees over time. In DLM's judgment, the fact that this increase is identified as a "surcharge" does not make a difference in applying the Local Mandate Law. In summary, since the obligation to pay registry of deeds recording fees predates 1980, it is DLM's opinion that the Local Mandate Law does not apply to the Community Preservation Act.



Financial Impact of the Payments in Lieu of Taxes Appropriation on Cities and Towns

Valuation of Chapter 58 State-Owned Land

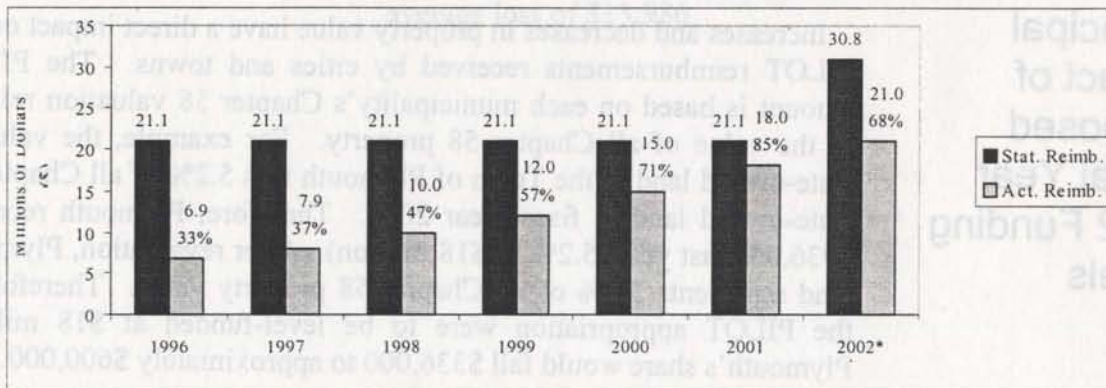
Payments in lieu of taxes (PILOT) for state-owned land have been provided to host municipalities since 1910. Under Sections 13-17 of Chapter 58, MGLs, the PILOT amount due each of 285 municipalities is calculated by applying an equalized (statewide) property tax rate to the fair cash value of state-owned land, as determined by the Department of Revenue (DOR). Only land is assessed, since the value of buildings and other improvements is statutorily excluded from PILOT reimbursements. The valuations are based on an appraisal conducted every five years by DOR, and municipalities aggrieved by DOR's determination of value may ask the Appellate Tax Board to determine the value. The Chapter 58 formula is shown below.

Chapter 58 PILOT Formula

	Valuation		Statewide Tax Rate		PILOT Amount
FY 2001	\$1.26 Billion	x	\$16.73 per \$1,000	=	\$21.1 Million
FY 2002	\$1.86 Billion	x	\$16.58 per \$1,000	=	\$30.8 Million

Underfunding

Underfunding of the PILOT account began in fiscal year 1989 during the state's financial crisis and continues today despite the General Court's efforts to gradually restore funding to the level provided by the Chapter 58 formula. In October 1994, DLM reported, that during the fiscal year period 1989-1995, cities and towns received \$51.8 million in reimbursements rather than the \$105.5 million called for by the statutory formula. This was approximately 50% of their entitlements, on average. In response, the General Court established a five-year schedule to achieve full funding of \$21 million by fiscal year 2002. (See Section 178 of Chapter 43 of the Acts of 1997.) Consequently, over the fiscal year period 1996-2001, cities and towns received \$69.8 million, or 55% of their entitlement of \$126.5 million under the statutory formula.



*House 1 & Legislative Budgets= \$18 Million (not shown)

Financial Impact of the Payments in Lieu of Taxes Appropriation on Cities and Towns

Revaluation

After five years of increases, the fiscal year 2002 budget appropriation for PILOT was to have matched the \$21 million called for by the statutory formula. However, the DOR revaluation of state-owned land, mandated by Section 13 of Chapter 58, found that the statewide value of Chapter 58 property increased from \$1.3 billion to \$1.8 billion, while the applicable state average property tax rate remained about the same at \$16.58 per thousand. If these variables affecting the Chapter 58 formula are used for fiscal year 2002 calculations, as they should be ($\$1.86 \text{ billion value} / \$1,000 \times \$16.58 = \30.8 million), annual reimbursements as currently proposed are not sufficient to fully compensate municipalities according to the Chapter 58 formula. Annual payments of approximately \$30.8 million would be required and would be applicable through fiscal year 2006.

Municipal Impact of Proposed Fiscal Year 2002 Funding Levels

Increases and decreases in property value have a direct impact on the PILOT reimbursements received by cities and towns. The PILOT amount is based on each municipality's Chapter 58 valuation relative to the value of all Chapter 58 property. For example, the value of state-owned land in the Town of Plymouth was 5.2% of all Chapter 58 state-owned land in fiscal year 2001. Therefore, Plymouth received \$936,000 last year (5.2% of \$18 million). After revaluation, Plymouth land represents 3.3% of all Chapter 58 property value. Therefore, if the PILOT appropriation were to be level-funded at \$18 million, Plymouth's share would fall \$336,000 to approximately \$600,000.

Please find below the summary financial impact of differing PILOT appropriations for fiscal year 2002.

Impact of level-funding PILOT at \$18 million as proposed by the fiscal year 2002 House Budget

- 131 municipalities would share gains totaling \$3.9 million. The average increase is \$29,737.
- 154 municipalities would receive lower PILOT payments, also equal to 3.9 million. The average loss is \$25,286.

Impact of fiscal year 2002 PILOT funding at \$21 million as proposed by the Senate Budget

- 163 municipalities would share gains totaling \$5.7 million with an average increase of \$35,226.
- 122 municipalities would share losses totaling \$2.74 million. The average loss is \$22,462.

Impact of fully funding PILOT according to the Chapter 58 formula for fiscal year 2002 - \$31 million.

- 237 municipalities would share gains totaling \$13.7 million. The average gain would be \$58,096.
- 48 municipalities would collectively lose \$767,342 for an average loss of \$15,986.

Office of the State Auditor Legislative Agenda

This section contains a summary of initiatives developed and filed by the OSA for the 2001/2002 legislative session. OSA bills either directly affect the OSA or address significant audit results and therefore complement audit recommendations by suggesting systemic improvements.

Municipal Impact of Proposed Fiscal Year 2002 Funding Levels

Increase and decreases in property value have a direct impact on the PILOT reimbursements received by cities and towns. The PILOT amount is based on each municipality's Chapter 58 valuation relative to the value of all Chapter 58 property. For example, the value of state-owned land in the Town of Plymouth was 5.2% of all Chapter 58 land owned land in fiscal year 2001. Therefore, Plymouth received \$936,000 last year (5.2% of \$18 million). After revaluation, Plymouth land represents 3.3% of all Chapter 58 property value. Therefore, if the PILOT appropriation were to be level-funded at \$18 million, Plymouth's share would fall \$336,000 to approximately \$600,000.

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Impact of level-funding PILOT at \$18 million as proposed by the fiscal year 2002 House Budget

- 131 municipalities would share gains totaling \$3.9 million. The average increase is \$29,757.
- 154 municipalities would receive lower PILOT payments, also equal to 3.9 million. The average loss is \$25,286.

House 3 An Act Relative to Production of Records for Review by the State Auditor

This bill would clarify language in the enabling statute of the OSA, which is meant to guarantee the State Auditor access to all records and documents pertinent to an ongoing audit. Under this legislation, the OSA would be authorized to issue a subpoena for the production of records to an auditee who refused repeated oral and written requests to make these materials available for review. This limited subpoena authority, which has already been granted to the House and Senate Post Audit Committees, the Inspector General's Office, and the Bureau of Accounts, is a valuable discretionary tool for improving the effectiveness and timeliness of the audit process.

House 3 has passed the House and is currently pending in the Senate.

House 4 An Act Clarifying the Scope of the Local Mandate Law

This bill would clarify the scope of municipal protection provided pursuant to Section 27C of Chapter 29, MGLs, the so-called Local Mandate Law. The statute provides that any law taking effect on or after January 1, 1981 that imposes any additional costs upon a city or town will be effective only if fully funded by the Commonwealth or if locally accepted. In addition, it provides that any post-1980 administrative regulation or law granting or increasing exemption from local taxation is not to be effective unless fully funded by the Commonwealth.

Certain court decisions over the past few years have both narrowed the scope of the Local Mandate Law's protection and created confusion. Consistent with the original intent of the law, House 4 would define "local mandate" to include post-1980 state laws and regulations that require a municipality to make additional expenditures to maintain any new or existing local activity, to undertake a service previously performed by the Commonwealth or a county, or to initiate or expand a contracted service. The bill also contains provisions that would allow for the reimbursement of legal costs incurred by a municipality in a successful mandate challenge and authorizes courts to grant an interim exemption from compliance. This bill would update the Local Mandate Law and establish a more useful standard for responding to local mandate issues.

House 4 is currently pending in the Joint Committee on Taxation.

House 5 An Act Providing for Uniform Administrative Standards in the Audit of Federal Aid Funds Received by State Agencies

This legislation would provide for uniform standards and overall coordination in the audit of federal aid funds. Under this bill, the OSA would receive notice from state agencies of federal aid funds to be audited, would assist agencies in setting the scope and standards for various kinds of audits, and would receive such audits when completed by private firms. The intent of the legislation is to ensure that agencies contract for and obtain audits that meet the requirements of all federal and state statutes and regulations and that audit duplication and expenses are reduced.

House 5 received a favorable report from the Joint Committee on State Administration and is currently pending before the House Committee on Ways and Means.

House 6 An Act Relative to Certain Requests for Local Audits

This bill would authorize the State Auditor to conduct audits of municipal departments if requested to do so by the governing or legislative body of a city or town. In recent years the Auditor has received an increasing number of such requests, which must be turned down because, under current law, the OSA cannot conduct audits of entities under the audit authority of the Bureau of Accounts within the Department of Revenue.

Currently, municipalities that want audit work, in addition to their required annual audit, can petition the Bureau of Accounts "to cause an audit to be made." Municipalities, under the direction of the Bureau, then contract for this work to be done on a limited basis by a private accounting firm. Although this procedure works well in most cases, there are instances in which municipal officials would like a particular review to be conducted by the State Auditor's Office. The Auditor would like to have the flexibility to respond positively to such requests.

House 6 received a favorable report from the Joint Committee on State Administration and is currently pending before the House Committee on Ways and Means.

House 7

An Act Providing for Review of Agency Fiscal Effect Statements by the State Auditor

This bill would amend Sections 2 and 3 of Chapter 30A, MGLs, by adding the State Auditor's Division of Local Mandates (DLM) to the listing of agencies to be notified of an upcoming hearing for any proposed regulation that may result in increased expenditures by a city, town, regional school district, or educational collaborative. It would also provide that the fiscal effect statement currently required by Section 5 of Chapter 30A related to the impact of proposed regulatory changes on municipalities and educational entities be filed with DLM.

House 7 would enhance the integrity of the fiscal effect process and ensure that the financial impact of proposed regulations on cities and towns is carefully considered with the current administrative process.

House 7 received a favorable report from the Joint Committee on State Administration and is currently pending before the House Committee on Ways and Means.

Private Occupational Schools: Financial Evaluations

Chapters 75C, 75D, and 93 of the Massachusetts General Laws require the Office of the State Auditor and the Department of Education to annually evaluate the financial and academic qualifications, respectively, of applicants for licensure or registration as private business, trade, or correspondence schools. Schools conducted by employers to train their employees and schools or colleges, chartered or otherwise authorized by the Commonwealth, are exempt from the mandate of the statutes. These consumer protection statutes were enacted to ensure that private occupational schools are both financially and academically qualified to operate in Massachusetts.

Prior to licensure or registration by the Department of Education, all such non-degree-granting business, trade, and correspondence schools are required to submit financial statements to the OSA. This information is evaluated to determine the solvency of each applicant. Those schools determined to be financially qualified for licensure or registration must then secure tuition protection in the amount recommended by the OSA.

Education Audits

AUDIT

ISSUE

DATE

1. Department
Parliamentary

Massachusetts statutes require the OSA to annually determine each school's appropriate tuition protection level, which may take the form of a surety bond, an irrevocable letter of credit, or a term deposit account payable to the Commonwealth. This consumer protection is intended to cover potential tuition refunds to students resulting from fraud, deceptive student recruitment practices, or a breach of contract by the school.

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At the close of fiscal year 2001, there were 173 active private occupational schools financially certified for Massachusetts licensure or registration. During the six-month period ended June 30, 2001, the OSA performed 69 financial evaluations. Seven schools represented first-time applicants, 62 reviews covered renewal applications, and four previously approved schools were reclassified as inactive.

2. Department
Information
3. Greenfield
Technical
4. University
Procurement

Programs of study offered by private occupational schools include appliance repair, broadcasting, business administration, computer skills, commercial art, fashion design, floral design, home health aide/certified nurses' assistant training, industrial technology, massage therapy, modeling, photography, plumbing, secretarial skills, sign painting, tractor trailer training, and ultrasound technology.

03/21/01

02/16/01

02/23/01

Appendix

Audit Reports Issued

Education Audits

AUDIT DATE	AUDIT NUMBER	AUDIT NUMBER	ISSUE DATE
1.	Department of Education-Community Partnerships for Children (CPC) Program (14 Entities) Department of Education Acton/Boxborough/Littleton CPC Attleboro CPC Berkshire Hills CPC Bourne CPC Chicopee CPC Falmouth CPC Fitchburg CPC Frontier R.S. CPC Greenfield CPC Peabody CPC Pittsfield CPC Salem CPC Worcester CPC	99-4067-3	01/11/01
2.	Department of Education-Expenditures for Information Technology	2000-4072-3	03/21/01
3.	Greenfield Community College-Information Technology & Financial-Related Controls	2001-0194-4C	02/16/01
4.	University of Massachusetts-Amherst Procurement Credit Card (Procard) Program	2000-0213-2	02/23/01

Human Services Audits

AUDIT DATE	AUDIT NUMBER	ISSUE DATE
1. Department of Public Health's Childhood Lead Poisoning Prevention Program	2001-0290-3	01/29/01
(34 Entities)		
Department of Public Health		
State Laboratory Institute		
32 Private Laboratories		
2. Fernald Developmental Center	2000-0267-3	04/20/01
3. Monson Developmental Center	2000-0262-3	01/30/01
4. Project Cope, Inc.	2000-4417-3	03/20/01
5. Soldiers' Home in Holyoke-Information Technology-Related Controls	2001-0064-4C	06/28/01
6. Soldiers' Home of Massachusetts/Chelsea	2001-0065-3	04/30/01
7. Tewksbury Hospital	2000-0304-2	06/26/01

Independent Authority Audits

AUDIT DATE	AUDIT NUMBER	AUDIT NUMBER	ISSUE DATE
1.	Brockton Redevelopment Authority	2001-3007-8	02/16/01
2.	Massachusetts Community Development Finance Corporation	2000-1022-3	04/30/01
3.	Massachusetts Technology Development Corporation	2000-0136-3	01/19/01
4.	Massachusetts Technology Park Corporation	2000-1304-3	02/05/01
5.	Massachusetts Turnpike Authority's Oversight Over Certain Design & Construction Activities Relating to the North/South Rail Link	99-4074-3	06/14/01
	(2 Entities)		
	Massachusetts Turnpike Authority		
	Massachusetts Bay Transportation Authority		
6.	Massachusetts Water Resources Authority- Outfall Tunnel/ Diffuser System	2001-4083-3	06/15/01
7.	Worcester Regional Transit Authority	2001-0880-3	03/30/01
18.	Southern Housing Authority	2001-0750-3	05/31/01
19.	Libridge Housing Authority	2001-0755-3	06/19/01
20.	West Bridgewater Housing Authority	2001-0815-3	01/31/01
21.	Yonkers Housing Authority	2001-0817-3	05/06/01

Judiciary/Law Enforcement Audits

AUDIT DATE	AUDIT NUMBER	AUDIT NUMBER	ISSUE DATE
1.	Barnstable County Superior Court	2000-1118-3	01/19/01
2.	Barnstable Superior Court, Clerk's Office- Transition Audit	2001-1118-2	06/28/01
3.	Cooperative Investigation with the Essex County District Attorney and the State Police Regarding an Embezzlement of Funds from the Andover Police Relief Association	2000-6006-9	02/27/01
4.	Massachusetts Correctional Institution at Cedar Junction-Information Technology Controls	2001-0152-4C	03/30/01
5.	Middlesex Division-Probate & Family Court Department	2001-1222-2	06/29/01
6.	Technical Assistance Provided to Northwestern District Attorney's Office-Town of Athol	2001-6008-9	01/31/01
7.	Worcester Sheriff's Department	2001-1423-3	06/26/01

Local Housing Authority Audits

AUDIT DATE	AUDIT NUMBER	AUDIT NUMBER	ISSUE DATE
1.	Auburn Housing Authority	2001-0605-3	03/30/01
2.	Brockton Housing Authority	2001-0621-3	06/19/01
3.	Cambridge Housing Authority-Information Technology and Financial Related Controls	2000-0626-4F	03/12/01
4.	Canton Housing Authority	2001-0628-3	03/28/01
5.	East Bridgewater Housing Authority	2001-0645-3	01/31/01
6.	Hamilton Housing Authority	2001-0671-3	06/29/01
7.	Hopkinton Housing Authority	2001-0681-3	04/30/01
8.	Lancaster Housing Authority	2001-0687-3	03/29/01
9.	Leicester Housing Authority	2001-0691-3	03/09/01
10.	Manchester Housing Authority	2001-0703-3	01/31/01
11.	Middleton Housing Authority	2001-0721-3	05/31/01
12.	Northborough Housing Authority	2001-0744-3	05/31/01
13.	Norwood Housing Authority	2001-0748-3	06/29/01
14.	Scituate Housing Authority	2001-0773-3	06/29/01
15.	Sharon Housing Authority	2001-0775-3	04/25/01
16.	Shrewsbury Housing Authority	2001-0776-3	04/20/01
17.	Southborough Housing Authority	2001-0875-3	04/20/01
18.	Southbridge Housing Authority	2001-0780-3	05/31/01
19.	Uxbridge Housing Authority	2001-0798-3	06/19/01
20.	West Bridgewater Housing Authority	2001-0810-3	01/31/01
21.	Whitman Housing Authority	2001-0817-3	05/08/01
22.	Worcester Housing Authority	2001-0818-3	05/08/01
23.	Worcester Housing Authority	2001-0819-3	05/08/01
24.	Worcester Housing Authority	2001-0820-3	05/08/01
25.	Worcester Housing Authority	2001-0821-3	05/08/01
26.	Worcester Housing Authority	2001-0822-3	05/08/01
27.	Worcester Housing Authority	2001-0823-3	05/08/01
28.	Worcester Housing Authority	2001-0824-3	05/08/01
29.	Worcester Housing Authority	2001-0825-3	05/08/01
30.	Worcester Housing Authority	2001-0826-3	05/08/01
31.	Worcester Housing Authority	2001-0827-3	05/08/01
32.	Worcester Housing Authority	2001-0828-3	05/08/01
33.	Worcester Housing Authority	2001-0829-3	05/08/01
34.	Worcester Housing Authority	2001-0830-3	05/08/01
35.	Worcester Housing Authority	2001-0831-3	05/08/01
36.	Worcester Housing Authority	2001-0832-3	05/08/01
37.	Worcester Housing Authority	2001-0833-3	05/08/01
38.	Worcester Housing Authority	2001-0834-3	05/08/01
39.	Worcester Housing Authority	2001-0835-3	05/08/01
40.	Worcester Housing Authority	2001-0836-3	05/08/01
41.	Worcester Housing Authority	2001-0837-3	05/08/01
42.	Worcester Housing Authority	2001-0838-3	05/08/01
43.	Worcester Housing Authority	2001-0839-3	05/08/01
44.	Worcester Housing Authority	2001-0840-3	05/08/01
45.	Worcester Housing Authority	2001-0841-3	05/08/01
46.	Worcester Housing Authority	2001-0842-3	05/08/01
47.	Worcester Housing Authority	2001-0843-3	05/08/01
48.	Worcester Housing Authority	2001-0844-3	05/08/01
49.	Worcester Housing Authority	2001-0845-3	05/08/01
50.	Worcester Housing Authority	2001-0846-3	05/08/01
51.	Worcester Housing Authority	2001-0847-3	05/08/01
52.	Worcester Housing Authority	2001-0848-3	05/08/01
53.	Worcester Housing Authority	2001-0849-3	05/08/01
54.	Worcester Housing Authority	2001-0850-3	05/08/01
55.	Worcester Housing Authority	2001-0851-3	05/08/01
56.	Worcester Housing Authority	2001-0852-3	05/08/01
57.	Worcester Housing Authority	2001-0853-3	05/08/01
58.	Worcester Housing Authority	2001-0854-3	05/08/01
59.	Worcester Housing Authority	2001-0855-3	05/08/01
60.	Worcester Housing Authority	2001-0856-3	05/08/01
61.	Worcester Housing Authority	2001-0857-3	05/08/01
62.	Worcester Housing Authority	2001-0858-3	05/08/01
63.	Worcester Housing Authority	2001-0859-3	05/08/01
64.	Worcester Housing Authority	2001-0860-3	05/08/01
65.	Worcester Housing Authority	2001-0861-3	05/08/01
66.	Worcester Housing Authority	2001-0862-3	05/08/01
67.	Worcester Housing Authority	2001-0863-3	05/08/01
68.	Worcester Housing Authority	2001-0864-3	05/08/01
69.	Worcester Housing Authority	2001-0865-3	05/08/01
70.	Worcester Housing Authority	2001-0866-3	05/08/01
71.	Worcester Housing Authority	2001-0867-3	05/08/01
72.	Worcester Housing Authority	2001-0868-3	05/08/01
73.	Worcester Housing Authority	2001-0869-3	05/08/01
74.	Worcester Housing Authority	2001-0870-3	05/08/01
75.	Worcester Housing Authority	2001-0871-3	05/08/01
76.	Worcester Housing Authority	2001-0872-3	05/08/01
77.	Worcester Housing Authority	2001-0873-3	05/08/01
78.	Worcester Housing Authority	2001-0874-3	05/08/0

Single Audits of Housing Authorities

AUDIT DATE	AUDIT NUMBER	AUDIT NUMBER	ISSUE DATE
1.	Abington Housing Authority	2000-3066-8	04/25/01
2.	Avon Housing Authority	2001-3049-8	06/29/01
3.	Barnstable Housing Authority	2001-3002-8	01/31/01
4.	Billerica Housing Authority	2001-3036-8	04/25/01
5.	Braintree Housing Authority	2001-3027-8	05/18/01
6.	Bridgewater Housing Authority	2000-3011-8	02/14/01
7.	Burlington Housing Authority	2001-3025-8	03/28/01
8.	Chelsea Housing Authority	2001-3017-8	04/25/01
9.	Chicopee Housing Authority	2001-3042-8	04/27/01
10.	Clinton Housing Authority	2001-3031-8	05/04/01
11.	Concord Housing Authority	2001-3041-8	04/26/01
12.	Danvers Housing Authority	2001-3028-8	04/26/01
13.	Dartmouth Housing Authority	2001-3001-8	02/14/01
14.	Dedham Housing Authority	2001-3026-8	05/04/01
15.	Easton Housing Authority	2001-3038-8	06/29/01
16.	Greenfield Housing Authority	2001-3024-8	02/14/01
17.	Haverhill Housing Authority	2001-3043-8	03/30/01
18.	Holden Housing Authority	2001-3032-8	01/31/01
19.	Ipswich Housing Authority	2001-3022-8	02/28/01
20.	Melrose Housing Authority	2000-3068-8	01/23/01
21.	Milford Housing Authority	2001-3035-8	03/22/01
22.	Milton Housing Authority	2000-3018-8	03/22/01
23.	Natick Housing Authority	2000-3064-8	01/23/01
24.	Newton Housing Authority	2000-3072-8	02/09/01
25.	Oxford Housing Authority	2001-3034-8	04/30/01
26.	Pembroke Housing Authority	2001-3005-8	04/30/01
27.	Pittsfield Housing Authority	2001-3033-8	04/27/01
28.	Reading Housing Authority	2001-3030-8	03/28/01
29.	Rockport Housing Authority	2001-3045-8	06/26/01
30.	Salisbury Housing Authority	2000-3070-8	01/31/01
31.	Springfield Housing Authority	2001-3021-8	06/29/01
32.	Warren Housing Authority	2000-3023-8	02/09/01
33.	Watertown Housing Authority	2000-3074-8	02/14/01
34.	Wayland Housing Authority	2001-3044-8	05/04/01
35.	Wellesley Housing Authority	2001-3003-1	04/18/01
36.	West Springfield Housing Authority	2000-3021-8	02/28/01
37.	Westfield Housing Authority	2000-3015-8	01/31/01
38.	Worcester Housing Authority	2001-3020-8	03/22/01

Other Audits

AUDIT DATE	AUDIT NUMBER	AUDIT NUMBER	ISSUE DATE
1.	Abolition of Berkshire County Government and the Transfer of its Functions, Assets, and Liabilities to the Commonwealth of Massachusetts (6 Entities) Berkshire County Treasurer's Office Berkshire County Sheriff's Department and Correctional Center Berkshire County Commissioner's Office Three Berkshire County Registries of Deeds	2001-5080-2	06/26/01
2.	Agency Compliance with the State Comptroller's Policies and the Massachusetts General Laws and Regulations: Selected Transaction Testing (9 Entities) Administrative Office of the Trial Court Attorney General's Office Department of Correction Department of Mental Retardation Division of Employment & Training Division of Health Care, Finance & Policy Executive Office of Public Safety Human Resources Division Northern Essex Community College	2001-5007-2	01/31/01
3.	Appellate Tax Board	99-0143-3	05/09/01
4.	Board of Registration in Medicine-Information Technology-Related Controls	2001-0117-4C	06/28/01
5.	Board of Registration of Cosmetology (2 Entities) Board of Registration of Cosmetology Division of Professional Licensure (formerly Division of Registration)	2000-0114-3	06/19/01
6.	Central Artery/Third Harbor Tunnel Project: Route I-90/Route 1-A Interchange and MBTA Airport Station Contracts	2001-4424-3	04/23/01

Other Audits

AUDIT DATE	AUDIT NUMBER	AUDIT NUMBER	ISSUE DATE
7.	Central Artery/Third Harbor Tunnel Project's Management Controls over Contractual Documentation Relating to the Wrap-Up Insurance Program	2001-4081-3	03/20/01
8.	Department of Environmental Protection's Community Septic Management Program	2000-5060-3	06/13/01
	(31 Entities)		
	Department of Environmental Protection		
	Department of Revenue/Division of Local Services		
	Water Pollution Abatement Trust (Includes 28 Communities):		
	Amherst		
	Ashburnham		
	Barnstable		
	Bellingham		
	East Bridgewater		
	Brookfield		
	Chesterfield		
	Concord		
	Dudley		
	Falmouth		
	Gloucester		
	Greenfield		
	Haverhill		
	Hudson		
	Littleton		
	Lunenburg		
	Medway		
	Mendon		
	Merrimac		
	Natick		
	Northborough		
	Paxton		
	Southborough		
	Tisbury		
	Townsend		
	West Boylston		
	Wayland		
	Westford		

Other Audits

AUDIT	AUDIT NUMBER	ISSUE DATE
9. Department of the State Treasurer and Receiver-General	2000-0085-3	02/07/01
10. Division of Insurance	2000-0101-5	02/20/01
11. Division of Occupational Safety Chapter 647 Review	2000-0217-2	03/29/01
12. Group Insurance Commission: Information Technology-Related Controls	2000-0040-4C	03/30/01
13. Health Care Security Trust	2001-1451-2	05/25/01
14. Massachusetts Highway Department: Information Technology-Related Controls	2000-0506-4F	03/30/01
15. Massachusetts Highway Department-Chapter 647 Review-Payroll Theft	2001-0506-9	03/30/01
16. Massachusetts Highway Department-Information Technology-Related Controls	2001-0506-4F	06/28/01
17. Norfolk County Registry of Deeds-Transition Audit	2001-1355-2	06/27/01
18. Public Employee Retirement Administration Commission	99-1315-3	02/02/01
19. Quarry Hills Project (5 Entities) Quarry Hills Associates, Inc. Massachusetts Highway Department Metropolitan District Commission City of Quincy Town of Milton	2001-4078-3	06/04/01

